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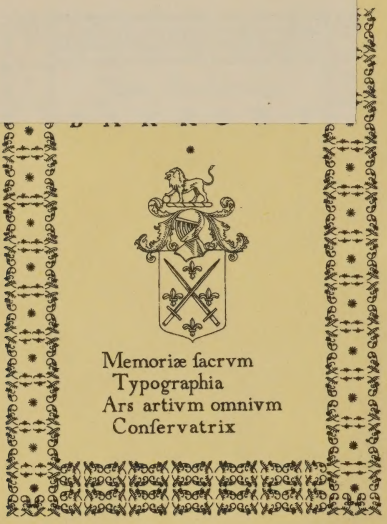

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THE WORKS OF

WALTER BAGEHOT

M. A., AND FELLOW OF UNIVERSITY COLLEGE, LONDON

WITH MEMOIRS BY R. H. HUTTON

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ADVERTISEMENT.

THE composition of this little book has occupied a much longer time than perhaps my readers may think its length or its importance deserves. It was begun as long ago as the autumn of 1870; and though its progress has been often suspended by pressing occupations and imperfect health, I have never ceased to work at it when I could. But I fear that in consequence, in some casual illustrations at least, every part of the book may not seem, as the lawyers would say, "to speak from the same time." The figures and the examples which it is most natural to use at one time are not quite those which it is most natural to use at another; and a slowly written book on a living and changing subject is apt a little to want unity in this respect.

I fear that I must not expect a very favorable reception for this work. It speaks mainly of four sets of persons, — the Bank of England, joint-stock banks other than that Bank, private bankers, and bill-brokers; and I am much afraid that neither will altogether like what is said of them. I can only say that the opinions now expressed have not been formed hastily or at a distance from the facts; that on the contrary, they have been slowly matured in "Lombard Street" itself; and that perhaps, as they

will not be altogether pleasing to any one, I may at least ask for the credit of having been impartial in my criticism.

I should also say that I am indebted to a friend for the correction of the final proof sheets, which an attack of illness prevented me from fully revising. If it had not been for his kind assistance, the publication of the book must have been postponed till the autumn; which, as its production has already been so slow, would have been very annoying to me.

WALTER BAGEHOT.

THE POPLARS, WIMBLEDON,
April 26, 1873.

LOMBARD STREET.

CHAPTER I.

INTRODUCTORY.

I VENTURE to call this essay "Lombard Street," and not "The Money Market" or any such phrase, because I wish to deal, and to show that I mean to deal, with concrete realities. A notion prevails that the money market is something so impalpable that it can only be spoken of in very abstract words, and that therefore books on it must always be exceedingly difficult; but I maintain that the money market is as concrete and real as anything else, that it can be described in as plain words, that it is the writer's fault if what he says is not clear. In one respect, however, I admit that I am about to take perhaps an unfair advantage. Half, and more than half, of the supposed "difficulty" of the money market has arisen out of the controversies as to "Peel's Act," and the abstract discussions on the theory on which that act is based or supposed to be based: but in the ensuing pages I mean to speak as little as I can of the Act of 1844; and when I do speak of it, I shall deal nearly exclusively with its experienced effects, and scarcely at all, if at all, with its refined basis.

For this I have several reasons: one, that if you say anything about the Act of 1844, it is little matter what else you say, for few will attend to it; most critics will seize on the passage as to the Act, either to attack it or defend it, as if it were the main

point. There has been so much fierce controversy as to this act of Parliament, and there is still so much animosity, that a single sentence respecting it is far more interesting to very many than a whole book on any other part of the subject. Two hosts of eager disputants on this subject ask of every new writer the one question, Are you with us or against us? and they care for little else. Of course, if the Act of 1844 really were, as is commonly thought, the *primum mobile* of the English money market, — the source of all good according to some, and the source of all harm according to others, — the extreme irritation excited by an opinion on it would be no reason for not giving a free opinion: a writer on any subject must not neglect its cardinal fact for fear that others may abuse him. But in my judgment the Act of 1844 is only a subordinate matter in the money market; what has to be said on it has been said at disproportionate length ; the phenomena connected with it have been magnified into greater relative importance than they at all deserve. We must never forget that a quarter of a century has passed since 1844, — a period singularly remarkable for its material progress, and almost marvelous in its banking development; even, therefore, if the facts so much referred to in 1844 had the importance then ascribed to them, — and I believe that in some respects they were even then overstated, — there would be nothing surprising in finding that in a new world, new phenomena had arisen which now are larger and stronger. In my opinion this is the truth : since 1844, Lombard Street is so changed that we cannot judge of it without describing and discussing a most vigorous adult world which then was small and weak. On this account I wish to say as little as is fairly possible of the Act of 1844, and as far as I can to isolate and dwell exclusively on the "Post-Peel" agencies; so that those who have had enough of that well-worn theme (and they are very many) may not be wearied, and that

the new and neglected parts of the subject may be seen as they really are.

The briefest and truest way of describing Lombard Street is to say that it is by far the greatest combination of economical power and economical delicacy that the world has ever seen. Of the greatness of the power there will be no doubt: money is economical power; every one is aware that England is the greatest moneyed country in the world, every one admits that it has much more immediately disposable and ready cash than any other country. But very few persons are aware *how much* greater the ready balance — the floating loan fund which can be lent to any one or for any purpose — is in England than it is anywhere else in the world. A very few figures will show how large the London loan fund is, and how much greater it is than any other. The known deposits — the deposits of banks which publish their accounts — are, in

	£
London (31st December, 1872), . . .	120,000,000
Paris (27th February, 1873), ...	13,000,000
New York (February, 1873), ...	40,000,000
German Empire (31st January, 1873), . .	8,000,000

And the unknown deposits — the deposits in banks which do not publish their accounts — are in London much greater than those in any other of these cities. The bankers' deposits of London are many times greater than those of any other city, those of Great Britain many times greater than those of any other country.

Of course the deposits of bankers are not a strictly accurate measure of the resources of a money market: on the contrary, much more cash exists out of banks in France and Germany, and in all non-banking countries, than could be found in England or Scotland, where banking is developed; but that cash is not, so to speak, "money-market money," — it is not attainable. Nothing but their

immense misfortunes, nothing but a vast loan in their own securities, could have extracted the hoards of France from the custody of the French people; the offer of no other securities would have tempted them, for they had confidence in no other securities; for all other purposes, the money hoarded was useless and might as well not have been hoarded. But the English money is "borrowable" money: our people are bolder in dealing with their money than any Continental nation; and even if they were not bolder, the mere fact that their money is deposited in a bank makes it far more obtainable. A million in the hands of a single banker is a great power, — he can at once lend it where he will, and borrowers can come to him because they know or believe that he has it; but the same sum scattered in tens and fifties through a whole nation is no power at all, — no one knows where to find it or whom to ask for it. Concentration of money in banks, though not the sole cause, is the principal cause which has made the money market of England so exceedingly rich, so much beyond that of other countries.

The effect is seen constantly: we are asked to lend, and do lend, vast sums which it would be impossible to obtain elsewhere. It is sometimes said that any foreign country can borrow in Lombard Street *at a price:* some countries can borrow much cheaper than others; but all, it is said, can have some money if they choose to pay enough for it. Perhaps this is an exaggeration; but confined, as of course it was meant to be, to civilized governments, it is not much of an exaggeration, — there are very few civilized governments that could not borrow considerable sums of us if they choose, and most of them seem more and more likely to choose. If any nation wants even to make a railway, — especially at all a poor nation, — it is sure to come to this country, to the country of banks, for the money. It is true that English bankers are not themselves very great

lenders to foreign states, but they are great lenders to those who lend: they advance on foreign stocks, as the phrase is, with "a margin,"—that is, they find eighty per cent. of the money, and the nominal lender finds the rest; and it is in this way that vast works are achieved with English aid which but for that aid would never have been planned.

In domestic enterprises it is the same. We have entirely lost the idea that any undertaking likely to pay, and seen to be likely, can perish for want of money; yet no idea was more familiar to our ancestors, or is more common now in most countries. A citizen of London in Queen Elizabeth's time could not have imagined our state of mind: he would have thought that it was of no use inventing railways (if he could have understood what a railway meant), for you would not have been able to collect the capital with which to make them. At this moment, in colonies and all rude countries, there *is* no large sum of transferable money; there is no fund from which you can borrow, and out of which you can make immense works. Taking the world as a whole, either now or in the past, it is certain that in poor states there is no spare money for new and great undertakings; and that in most rich states the money is too scattered, and clings too close to the hands of the owners, to be often obtainable in large quantities for new purposes. A place like Lombard Street, where in all but the rarest times money can be always obtained, upon good security or upon decent prospects of probable gain, is a luxury which no country has ever enjoyed with even comparable equality before.

But though these occasional loans to new enterprises and foreign states are the most conspicuous instances of the power of Lombard Street, they are not by any means the most remarkable or the most important use of that power: English trade is carried on upon borrowed capital to an extent of which few

foreigners have an idea, and none of our ancestors could have conceived. In every district small traders have arisen who "discount their bills" largely, and with the capital so borrowed, harass and press upon, if they do not eradicate, the old capitalist. The new trader has obviously an immense advantage in the struggle of trade. If a merchant have £50,000 all his own, to gain 10 per cent. on it he must make £5,000 a year, and must charge for his goods accordingly; but if another has only £10,000, and borrows £40,000 by discounts (no extreme instance in our modern trade), he has the same capital of £50,000 to use, and can sell much cheaper. If the rate at which he borrows be 5 per cent., he will have to pay £2,000 a year; and if, like the old trader, he make £5,000 a year, he will still, after paying his interest, obtain £3,000 a year, or 30 per cent. on his own £10,000. As most merchants are content with much less than 30 per cent., he will be able, if he wishes, to forego some of that profit, lower the price of the commodity, and drive the old-fashioned trader—the man who trades on his own capital—out of the market. In modern English business, owing to the certainty of obtaining loans on discount of bills or otherwise at a moderate rate of interest, there is a steady bounty on trading with borrowed capital, and a constant discouragement to confine yourself solely or mainly to your own capital.

This increasingly democratic structure of English commerce is very unpopular in many quarters, and its effects are no doubt exceedingly mixed. On the one hand, it prevents the long duration of great families of merchant princes, such as those of Venice and Genoa, who inherited nice cultivation as well as great wealth, and who, to some extent, combined the tastes of an aristocracy with the insight and *verve* of men of business. These are pushed out, so to say, by the dirty crowd of little men; after a generation or two they retire into idle luxury. Upon their immense

capital they can only obtain low profits, and these they do not think enough to compensate them for the rough companions and rude manners they must meet in business. This constant leveling of our commercial houses is, too, unfavorable to commercial morality. Great firms, with a reputation which they have received from the past and which they wish to transmit to the future, cannot be guilty of small frauds: they live by a *continuity* of trade, which detected fraud would spoil. When we scrutinize the reason of the impaired reputation of English goods, we find it is the fault of new men with little money of their own, created by bank "discounts": these men want business at once, and they produce an inferior article to get it; they rely on cheapness, and rely successfully.

But these defects and others in the democratic structure of commerce are compensated by one great excellence: no country of great hereditary trade, no European country at least, was ever so little "sleepy," to use the only fit word, as England; no other was ever so prompt at once to seize new advantages. A country dependent mainly on great "merchant princes" will never be so prompt; their commerce perpetually slips more and more into a commerce of routine. A man of large wealth, however intelligent, always thinks, more or less, "I have a great income, and I want to keep it: if things go on as they are I shall certainly keep it, but if they change I *may* not keep it;" consequently he considers every change of circumstance a "bore," and thinks of such changes as little as he can. But a new man, who has his way to make in the world, knows that such changes are his opportunities; he is always on the lookout for them, and always heeds them when he finds them. The rough and vulgar structure of English commerce is the secret of its life; for it contains the "propensity to variation," which, in the social as in the animal kingdom, is the principle of progress.

In this constant and chronic borrowing, Lombard Street is the great go-between; it is a sort of standing broker between [the] quiet saving districts of the country and the active employing districts. Why particular trades settled in particular places it is often difficult to say: but one thing is certain, that when a trade *has* settled in any one spot, it is very difficult for another to oust it, — impossible unless the second place possesses some very great intrinsic advantage; commerce is curiously conservative in its homes, unless it is imperiously obliged to migrate. Partly from this cause, and partly from others, there are whole districts in England which cannot and do not employ their own money. No purely agricultural county does so; the savings of a county with good land but no manufactures and no trade much exceed what can be safely lent in the county. These savings are first lodged in the local banks, are by them sent to London, and are deposited with London bankers or with the bill-brokers. In either case the result is the same: the money thus sent up from the accumulating districts is employed in discounting the bills of the industrial districts. Deposits are made with the bankers and bill-brokers in Lombard Street by the bankers of such counties as Somersetshire and Hampshire, and those bill brokers and bankers employ them in the discount of bills from Yorkshire and Lancashire. Lombard Street is thus a perpetual agent between the two great divisions of England, — between the rapidly growing districts, where almost any amount of money can be well and easily employed, and the stationary and the declining districts, where there is more money than can be used.

This organization is so useful because it is so easily adjusted. Political economists say that capital sets towards the most profitable trades, and that it rapidly leaves the less profitable and non-paying trades; but in ordinary countries this is a slow process, and some persons who want to have ocular demonstration

of abstract truths have been inclined to doubt it because they could not see it. In England, however, the process would be visible enough if you could only see the books of the bill-brokers and the bankers: their bill cases as a rule are full of the bills drawn in the most profitable trades, and *cæteris paribus* and in comparison empty of those drawn in the less profitable. If the iron trade ceases to be as profitable as usual, less iron is sold; the fewer the sales the fewer the bills: and in consequence the number of iron bills in Lombard Street is diminished. On the other hand, if in consequence of a bad harvest the corn trade becomes on a sudden profitable, immediately "corn bills" are created in great numbers, and if good are discounted in Lombard Street. Thus English capital runs as surely and instantly where it is most wanted, and where there is most to be made of it, as water runs to find its level.

This efficient and instantly ready organization gives us an enormous advantage in competition with less advanced countries, — less advanced, that is, in this particular respect of credit. In a new trade, English capital is instantly at the disposal of persons capable of understanding the new opportunities and of making good use of them. In countries where there is little money to lend, and where that little is lent tardily and reluctantly, enterprising traders are long kept back, because they cannot at once borrow the capital without which skill and knowledge are useless. All *sudden* trades come to England, and in so doing often disappoint both rational probability and the predictions of philosophers. The Suez Canal is a curious case of this: all predicted that the canal would undo what the discovery of the passage to India round the Cape effected. Before that, all Oriental trade went to ports in the South of Europe, and was thence diffused through Europe. That London and Liverpool should be centers of East-Indian commerce is a geographical anomaly, which the Suez

Canal, it was said, would rectify: "The Greeks," said M. de Tocqueville, "the Styrians, the Dalmatians, the Italians, and the Sicilians are the people who will use the canal, if any use it."* But on the contrary, the main use of the canal has been by the English: none of the nations named by Tocqueville had the capital, or a tithe of it, ready to build the large screw steamers which alone can use the canal profitably. Ultimately these plausible predictions may or may not be right, but as yet they have been quite wrong; not because England has rich people, — there are wealthy people in all countries, — but because she possesses an unequaled fund of floating money, which will help in a moment any merchant who sees a great prospect of new profit.

And not only does this unconscious "organization of capital," to use a Continental phrase, make the English specially quick in comparison with their neighbors on the Continent at seizing on novel mercantile opportunities, but it makes them likely also to retain any trade on which they have once regularly fastened. Mr. MacCulloch, following Ricardo, used to teach that all old nations had a special aptitude for trades in which much capital is required: the interest of capital having been reduced in such countries, he argued, by the necessity of continually resorting to inferior soils, they can undersell countries where profit is high, in all trades needing great capital.† And in this theory there is doubtless much truth, though it can only be applied in practice after a number of limitations and with a number of deductions of which the older school of political economists did not take enough notice; but the same principle plainly and practically applies to England, in consequence of her habitual use of borrowed capital. As has been

* Conversation with Senior, May 15, 1857; Vol. ii. of De T.'s "Remains."

† Note vii. to MacCulloch's edition of the "Wealth of Nations" (pages 475–7); criticizing also Ricardo's chapter on "Profits" (vi. of "Political Economy").

explained, a new man, with a small capital of his own and a large borrowed capital, can undersell a rich man who depends on his own capital only: the rich man wants the full rate of mercantile profit on the whole of the capital employed in his trade, but the poor man wants only the interest of money (perhaps not a third of the rate of profit) on very much of what *he* uses, and therefore an income will be an ample recompense to the poor man which would starve the rich man out of the trade. All the common notions about the new competition of foreign countries with England, and its dangers, — notions in which there is in other aspects much truth, — require to be reconsidered in relation to this aspect: England has a special machinery for getting into trade new men who will be content with low prices; and this machinery will probably secure her success, for no other country is soon likely to rival it effectually.

There are many other points which might be insisted on, but it would be tedious and useless to elaborate the picture. The main conclusion is very plain: that English trade is become essentially a trade on borrowed capital, and that it is only by this refinement of our banking system that we are able to do the sort of trade we do, or to get through the quantity of it.

But in exact proportion to the power of this system is its delicacy, — I should hardly say too much if I said its danger; only our familiarity blinds us to the marvelous nature of the system. There never was so much borrowed money collected in the world as is now collected in London. Of the many millions in Lombard Street, infinitely the greater proportion is held by bankers or others on short notice or on demand, — that is to say, the owners could ask for it all any day they please; in a panic some of them do ask for some of it: if any large fraction of that money really was demanded, our banking system and our industrial system too would be in great danger.

Some of those deposits, too, are of a peculiar and very distinct nature. Since the Franco-German war, we have become to a much larger extent than before the bankers of Europe; a very large sum of foreign money is on various accounts and for various purposes held here: and in a time of panic it might be asked for. In 1866 we held only a much smaller sum of foreign money, but that smaller sum was demanded and we had to pay it at great cost and suffering; and it would be far worse if we had to pay the greater sums we now hold, without better resources than we had then.

It may be replied that though our instant liabilities are great, our present means are large; that though we have much we may be asked to pay at any moment, we have very much always ready to pay it with. But on the contrary, there is no country at present, and there never was any country before, in which the ratio of the cash reserve to the bank deposits was so small as it is now in England.* So far from our being able to rely on the proportional magnitude of our cash in hand, the amount of that cash is so exceedingly small that a bystander almost trembles when he compares its minuteness with the immensity of the credit which rests upon it.

Again, it may be said that we need not be alarmed at the magnitude of our credit system or at its refinement, for that we have learned by experience the way of controlling it, and always manage it with discretion. But we do *not* always manage it with discretion: there is the astounding instance of Overend, Gurney & Co. to the contrary. Ten years ago that house stood next to the Bank of England in the City of London; it was better known abroad than any similar firm,—known perhaps better than any purely English firm. The partners had great estates, which had mostly been made in the business; they still derived an immense income from it: yet

*See Note A in Appendix.

in six years they lost all their own wealth, sold the business to the company, and then lost a large part of the company's capital; and these losses were made in a manner so reckless and so foolish that one would think a child who had lent money in the City of London would have lent it better. After this example, we must not confide too surely in long-established credit, or in firmly rooted traditions of business; we must examine the system on which these great masses of money are manipulated, and assure ourselves that it is safe and right.

But it is not easy to rouse men of business to the task: they let the tide of business float before them; they make money or strive to do so while it passes, and they are unwilling to think where it is going. Even the great collapse of Overends, though it caused a panic, is beginning to be forgotten. Most men of business think, "Anyhow, this system will probably last my time: it has gone on a long time, and is likely to go on still." But the exact point is, that it has *not* gone on a long time; the collection of these immense sums in one place and in few hands is perfectly new. In 1844 the liabilities of the four great London joint-stock banks were £10,637,000, they now are more than £60,000,000; the private deposits of the Bank of England then were £9,000,000, they now are £18,000,000; there was in 1844 throughout the country but a fraction of the vast deposit business which now exists. We cannot appeal, therefore, to experience to prove the safety of our system as it now is, for the present magnitude of that system is entirely new. Obviously, a system may be fit to regulate a few millions and yet quite inadequate when it is set to cope with many millions; and thus it *may* be with "Lombard Street," so rapid has been its growth and so unprecedented is its nature.

I am by no means an alarmist. I believe that our system, though curious and peculiar, may be worked safely; but if we wish so to work it, we must study

it. We must not think we have an easy task when we have a difficult task, or that we are living in a natural state when we are really living in an artificial one. Money will not manage itself, and Lombard Street has a great deal of money to manage.

CHAPTER II.

A GENERAL VIEW OF LOMBARD STREET.

I.

THE objects which you see in Lombard Street, and in that money world which is grouped about it, are the Bank of England, the private banks, the joint-stock banks, and the bill-brokers. But before describing each of these separately, we must look at what all have in common and at the relation of each to the others.

The distinctive function of the banker, says Ricardo, begins as soon as he uses the money of *others;** as long as he uses his own money he is only a capitalist. Accordingly, all the banks in Lombard Street (and bill-brokers are for this purpose only a kind of bankers) hold much money belonging to other people, on running account and on deposit. In Continental language, Lombard Street is an organization of credit; and we are to see if it is a good or bad organization in its kind, or, if (as is most likely) it turn out to be mixed, what are its merits and what are its defects.

The main point on which one system of credit differs from another is "soundness." Credit means that a certain confidence is given and a certain trust reposed: Is that trust justified? and, Is that confidence wise? these are the cardinal questions. To put it more simply, credit is a set of promises to pay: will those promises be kept? Especially in banking, where the "liabilities," or promises to pay, are so

* "Proposals for an Economical and Secure Currency;" MacCulloch's edition, page 431.

large, and the time at which to pay them if exacted is so short, an instant capacity to meet engagements is the cardinal excellence.

All which a banker wants to pay his creditors is a sufficient supply of the *legal tender* of the country, no matter what that legal tender may be. Different countries differ in their laws of legal tender; but for the primary purposes of banking these systems are not material. A good system of currency will benefit the country, and a bad system will hurt it: indirectly, bankers will be benefited or injured with the country in which they live; but practically, and for the purposes of their daily life, they have no need to think and never do think on theories of currency. They look at the matter simply; they say, "I am under an obligation to pay such and such sums of legal currency: how much have I in my till, or have I at once under my command, of that currency?" In America, for example, it is quite enough for a banker to hold "greenbacks," though the value of these changes as the government chooses to enlarge or contract the issue. But a practical New York banker has no need to think of the goodness or badness of this system at all; he need only keep enough "greenbacks" to pay all probable demands, and then he is fairly safe from the risk of failure.

By the law of England the legal tenders are gold and silver coin (the last for small amounts only), and Bank of England notes; but the number of our attainable bank notes is not, like American "greenbacks," dependent on the will of the state, — it is limited by the provisions of the Act of 1844. That act separates the Bank of England into two halves: the Issue Department only issues notes, and can only issue £15,000,000 on government securities; for all the rest it must have bullion deposited. Take for example an account which may be considered an average specimen of those of the last few years, — that for the last week of 1869: —

An account pursuant to the Act 7th and 8th Victoria, cap. 32, *for the week ending on Wednesday, the 29th day of December*, 1869.

ISSUE DEPARTMENT.

	£		£
Notes issued, . . .	33,288,640	Government debt, . .	11,015,100
		Other securities, . .	3,984,900
		Gold coin and bullion,	18,288,640
		Silver bullion, . . .	—
	33,288,640		33,288,640

BANKING DEPARTMENT.

	£		£
Proprietors' capital, .	14,553,000	Government securities,	13,811,953
Rest, ...	3,103,301	Other securities, . .	19,781,988
Public deposits, including Exchequer, Savings Banks, Commissioners of National Debt, and dividend accounts, ...	8,585,215	Notes, ...	10,389,690
		Gold and silver coin, .	907,982
Other deposits, . . .	18,204,607		
Seven-day and other bills, ...	445,490		
	44,891,613		44,891,613

GEO. FORBES, *Chief Cashier.*

Dated the 30th December, 1869.

There are here £15,000,000 bank notes issued on securities, and £18,288,640 represented by bullion. The Bank of England has no power, by law, to increase the currency in any other manner; it holds the stipulated amount of securities, and for all the rest it must have bullion. This is the "cast-iron" system, — the "hard and fast" line which the opponents of the Act say ruins us, and which the partisans of the Act say saves us; but I have nothing to do with its expediency here, — all which is to my purpose is that our paper "legal tender," our bank notes, can only be

obtained in this manner. If therefore an English banker retains a sum of Bank of England notes or coin in due proportion to his liabilities, he has a sufficient amount of the legal tender of this country, and he need not think of anything more.

But here a distinction must be made. It is to be observed that properly speaking we should not include in the "reserve" of a bank, "legal tenders" or cash which the bank keeps to transact its daily business, — that is as much a part of its daily stock in trade as its desks or offices; or at any rate, whatever words we may choose to use, we must carefully distinguish between this cash in the till which is wanted every day, and the *safety* fund, as we may call it, — the special reserve held by the bank to meet extraordinary and unfrequent demands.

What, then, subject to this preliminary explanation, is the amount of legal tender held by our bankers against their liabilities? The answer is remarkable, and is the key to our whole system: it may be broadly said that no bank, in London or out of it, holds any considerable sum in hard cash or legal tender (above what is wanted for its daily business), except the Banking Department of the Bank of England. That department had on the 29th day of December, 1869, liabilities as follows: —

	£
Public deposits, ...	8,585,000
Private deposits, ...	18,205,000
Seven-day and other bills, ...	445,000
Total, ...	27,235,000

and a cash reserve of £11,297,000. And this is all the cash reserve, we must carefully remember, which under the law the Banking Department of the Bank of England, as we cumbrously call it, — the Bank of England for banking purposes, — possesses; that department can no more multiply or manufacture bank notes than any other bank can multiply them. At that particular day the Bank of England had only

£11,297,000 in its till, against liabilities of nearly three times the amount. It had "consols" and other securities which it could offer for sale, no doubt, and which if sold would augment its supply of bank notes, — and the relation of such securities to real cash will be discussed presently; but of real cash, the Bank of England for *this* purpose — the banking Bank — had then so much and no more.

And we may well think this a great deal, if we examine the position of other banks: no other bank holds any amount of substantial importance in its own till beyond what is wanted for daily purposes. All London banks keep their principal reserve on deposit at the Banking Department of the Bank of England; this is by far the easiest and safest place for them to use, — the Bank of England thus has the responsibility of taking care of it. The same reasons which make it desirable for a private person to keep a banker make it also desirable for every banker, as respects his reserve, to bank with another banker if he safely can. The custody of very large sums in solid cash entails much care and some cost; every one wishes to shift these upon others if he can do so without suffering: accordingly, the other bankers of London, having perfect confidence in the Bank of England, get that Bank to keep their reserve for them.

The London bill-brokers do much the same. Indeed, they are only a special sort of bankers, who allow daily interest on deposits and who for most of their money give security; but we have no concern now with these differences of detail. The bill-brokers lend most of their money, and deposit the remnant either with the Bank of England or some London banker; that London banker lends what he chooses of it, the rest he leaves at the Bank of England: you always come back to the Bank of England at last.

But those who keep immense sums with a banker gain a convenience at the expense of a danger: they

are liable to lose them if the bank fail. As all other bankers keep their banking reserve at the Bank of England, they are liable to fail if it fails; they are dependent on the management of the Bank of England, in a day of difficulty and at a crisis, for the spare money they keep to meet that difficulty and crisis. And in this there is certainly considerable risk: three times "Peel's Act" has been suspended because the Banking Department was empty. Before the act was broken

	£
In 1847, the Banking Department was reduced to	1,994,000
1857, " "	1,462,000
1866, " "	3,000,000

In fact, in none of those years could the Banking Department of the Bank of England have survived if the law had not been broken.

Nor must it be fancied that this danger is unreal, artificial, and created by law. There is a risk of our thinking so, because we hear that the danger can be cured by breaking an act; but substantially the same danger existed before the act. In 1825, when only coin was a legal tender, and when there was only one department in the Bank, the Bank had reduced its reserve to £1,027,000, and was within an ace of stopping payment.

But the danger to the depositing banks is not the sole or the principal consequence of this mode of keeping the London reserve: the main effect is, to cause the reserve to be much smaller in proportion to the liabilities than it would otherwise be,—the reserve of the London bankers being on deposit in the Bank of England, the Bank always lends a principal part of it. Suppose (a favorable supposition) that the Banking Department holds more than two-fifths of its liabilities in cash, that it lends three-fifths of its deposits and retains in reserve only two-fifths; if then the aggregate of the bankers' deposited reserve be £5,000,000, £3,000,000 of it will be lent by the

Banking Department, and £2,000,000 will be kept in the till: in consequence, that £2,000,000 is all which is really held in actual cash as against the liabilities of the depositing banks; if Lombard Street were on a sudden thrown into liquidation, and made to pay as much as it could on the spot, that £2,000,000 would be all which the Bank of England could pay to the depositing banks, and consequently all, besides the small cash in the till, which those banks could on a sudden pay to the persons who have deposited with them.

We see then that the banking reserve of the Bank of England — some £10,000,000 on an average of years now, and formerly much less — is all which is held against the liabilities of Lombard Street; and if that were all, we might well be amazed at the immense development of our credit system, — in plain English, at the immense amount of our debts payable on demand, and the smallness of the sum of actual money which we keep to pay them if demanded. But there is more to come: Lombard Street is not only a place requiring to keep a reserve, it is itself a place where reserves are kept. All country bankers keep their reserve in London; they only retain in each country town the minimum of cash necessary to the transaction of the current business of that country town. Long experience has told them to a nicety how much this is, and they do not waste capital and lose profit by keeping more idle; they send the money to London, invest a part of it in securities, and keep the rest with the London bankers and the bill-brokers. The habit of Scotch and Irish bankers is much the same: all their spare money is in London, and is invested as all other London money now is: and therefore the reserve in the Banking Department of the Bank of England is the banking reserve not only of the Bank of England, but of all London; and not only of all London, but of all England, Ireland, and Scotland too.

Of late there has been a still further increase in our liabilities: since the Franco-German war we may be said to keep the European reserve also. Deposit banking is indeed so small on the Continent that no large reserve need be held on account of it; a reserve of the same sort which is needed in England and Scotland is not needed abroad: but all great communities have at times to pay large sums in cash, and of that cash a great store must be kept somewhere. Formerly there were two such stores in Europe, — one was the Bank of France, and the other the Bank of England; but since the suspension of specie payments by the Bank of France, its use as a reservoir of specie is at an end, — no one can draw a check on it and be sure of getting gold or silver for that check: accordingly, the whole liability for such international payments in cash is thrown on the Bank of England. No doubt foreigners cannot take from us *our own* money, — they must send here "value" in some shape or other for all they take away; but they need not send "cash," — they may send good bills and discount them in Lombard Street, and take away any part of the produce or all the produce in bullion. It is only putting the same point in other words to say that all exchange operations are centering more and more in London. Formerly for many purposes Paris was a European settling-house, but now it has ceased to be so. The note of the Bank of France has not indeed been depreciated enough to disorder ordinary transactions: but any depreciation, however small, — even the liability to depreciation without its reality, — is enough to disorder exchange transactions; they are calculated to such an extremity of fineness that the change of a decimal may be fatal, and may turn a profit into a loss. Accordingly, London has become the sole great settling-house of exchange transactions in Europe, instead of being [as] formerly one of two; and this pre-eminence London will probably maintain, for it

is a natural pre-eminence. The number of mercantile bills drawn upon London incalculably surpasses those drawn on any other European city; London is the place which receives more than any other place and pays more than any other place, and therefore it is the natural "clearing-house." The pre-eminence of Paris partly arose from a distribution of political power, which is already disturbed; but that of London depends on the regular course of commerce, which is singularly stable and hard to change.

Now that London is the clearing-house to foreign countries, London has a new liability to foreign countries. At whatever place many people have to make payments, at that place those people must keep money; a large deposit of foreign money in London is now necessary for the business of the world. During the immense payments from France to Germany, the sum *in transitu* — the sum in London — has perhaps been unusually large; but it will ordinarily be very great. The present political circumstances no doubt will soon change: we shall soon hold in Lombard Street far less of the money of foreign governments; but we shall hold more and more of the money of private persons, for the deposit at a clearing-house necessary to settle the balance of commerce must tend to increase as that commerce itself increases.

And this foreign deposit is evidently of a delicate and peculiar nature: it depends on the good opinion of foreigners, and that opinion may diminish or may change into a bad opinion. After the panic of 1866, especially after the suspension of Peel's Act (which many foreigners confound with a suspension of cash payments), a large amount of foreign money was withdrawn from London; and we may reasonably presume that in proportion as we augment the deposits of cash by foreigners in London, we augment both the chances and the disasters of a "run" upon England.

And if that run should happen, the bullion to meet it must be taken from the Bank: there is no other large store in the country. The great exchange dealers may have a little for their own purposes, but they have no store worth mentioning in comparison with this. If a foreign creditor is so kind as to wait his time and buy the bullion as it comes into the country, he may be paid without troubling the Bank or distressing the money market; the German government has recently been so kind,—it was in no respect afraid: but a creditor who takes fright will not wait, and if he wants bullion in a hurry he must come to the Bank of England.

In consequence, all our credit system depends on the Bank of England for its security; on the wisdom of the directors of that one joint-stock company it depends whether *England shall be solvent or insolvent.* This may seem too strong, but it is not: all banks depend on the Bank of England, and all merchants depend on some banker. If a merchant have £10,000 at his bankers, and want to pay it to some one in Germany, he will not be able to pay it unless his banker can pay him; and the banker will not be able to pay if the Bank of England should be in difficulties and cannot produce his "reserve."

The directors of the Bank are therefore, in fact if not in name, trustees for the public, to keep a banking reserve on their behalf; and it would naturally be expected either that they distinctly recognized this duty and engaged to perform it, or that their own self-interest was so strong in the matter that no engagement was needed. But so far from there being a distinct undertaking on the part of the Bank directors to perform this duty, many of them would scarcely acknowledge it, and some altogether deny it. Mr. Hankey, one of the most careful and most experienced of them, says in his book on the Bank of England, the best account of the practice and working of the Bank which anywhere exists:—"I do not

intend to enter here at any length on the subject of the general management of the Bank," meaning the Banking Department, "as the principle on which the business is carried on does not differ, so far as I know, from that of any well-conducted bank in London." But as any one can see by the published figures, the Banking Department of the Bank of England keeps as a great reserve in bank notes and coin between 30 and 50 per cent. of its liabilities, and the other banks only keep in bank notes and coin the bare minimum they need to open shop with; and such a constant difference indicates, I conceive, that the two are *not* managed on the same principle.

The practice of the Bank has, as we all know, been much and greatly improved; they do not now manage like the other banks in Lombard Street, — they keep an altogether different kind and quantity of reserve: but though the practice is mended, the theory is not. There has never been a distinct resolution passed by the directors of the Bank of England, and communicated by them to the public, stating even in the most general manner how much reserve they mean to keep or how much they do not mean, or by what principle in this important matter they will be guided.

The position of the Bank directors is indeed most singular. On the one side a great City opinion — a great national opinion, I may say, for the nation has learnt much from many panics — requires the directors to keep a large reserve; the newspapers, on behalf of the nation, are always warning the directors to keep it, and watching that they do keep it: but on the other hand, another less visible but equally constant pressure pushes the directors in exactly the reverse way, and inclines them to diminish the reserve.

This is the natural desire of all directors to make a good dividend for their shareholders. The more money lying idle, the less, *cæteris paribus*, is the

dividend; the less money lying idle, the greater is the dividend: and at almost every meeting of the proprietors of the Bank of England there is a conversation on this subject, — some proprietor says that he does not see why so much money is kept idle, and hints that the dividend ought to be more.

Indeed, it cannot be wondered at that the Bank proprietors do not quite like their position: theirs is the oldest bank in the City, but their profits do not increase, while those of other banks most rapidly increase. In 1844, the dividend on the stock of the Bank of England was 7 per cent., and the price of the stock itself 212; the dividend now is 9 per cent., and the price of the stock 232: but in the same time the shares of the London and Westminster Bank, in spite of an addition of 100 per cent. to the capital, have risen from 27 to 66, and the dividend from 6 per cent. to 20 per cent. That the Bank proprietors should not like to see other companies getting richer than their company is only natural.

Some part of the lowness of the Bank dividend, and of the consequent small value of Bank stock, is undoubtedly caused by the magnitude of the Bank capital; but much of it is also due to the great amount of unproductive cash — of cash which yields no interest — that the Banking Department of the Bank of England keeps lying idle. If we compare the London and Westminster Bank — which is the first of the joint-stock banks in the public estimation, and known to be very cautiously and carefully managed — with the Bank of England, we shall see the difference at once: the London and Westminster has only 13 per cent. of its liabilities lying idle, the Banking Department of the Bank of England has over 40 per cent. So great a difference in the management must cause, and does cause, a great difference in the profits. Inevitably, the shareholders of the Bank of England will dislike this great difference; more or less, they will always urge their directors

to diminish as far as possible the unproductive reserve, and to augment as far as possible their own dividend.

In most banks there would be a wholesome dread restraining the desire of the shareholders to reduce the reserve, — they would fear to impair the credit of the bank; but, fortunately or unfortunately, no one has any fear about the Bank of England. The English world at least believes that it will not, almost that it *cannot* fail. Three times since 1844 the Banking Department has received assistance, and would have failed without it; in 1825 the entire concern almost suspended payment, in 1797 it actually did so: but still there is a faith in the Bank, contrary to experience and despising evidence. No doubt in every one of these years the condition of the Bank, divided or undivided, was in a certain sense most sound: it could *ultimately* have paid all its creditors all it owed, and returned to its shareholders all their own capital. But ultimate payment is not what the creditors of a bank want: they want present, not postponed payment; they want to be repaid according to agreement; the contract was that they should be paid on demand, and if they are not paid on demand they may be ruined: and that instant payment, in the years I speak of, the Bank of England certainly could not have made. But no one in London ever dreams of questioning the credit of the Bank, and the Bank never dreams that its own credit is in danger; somehow everybody feels the Bank is sure to come right. In 1797, when it had scarcely any money left, the government said not only that it need not pay away what remained, but that it *must* not; the effect of "letters of license" to break Peel's Act has confirmed the popular conviction that the government is close behind the Bank, and will help it when wanted. Neither the Bank nor the Banking Department have ever had an idea of being put "into liquidation": most men would think as soon of "winding up" the English nation.

Since then the Bank of England, as a bank, is exempted from the perpetual apprehension that makes other bankers keep a large reserve, — the apprehension of discredit, — it would seem particularly necessary that its managers should be themselves specially interested in keeping that reserve, and specially competent to keep it. But I need not say that the Bank directors have not their personal fortune at stake in the management of the Bank, — they are rich City merchants, and their stake in the Bank is trifling in comparison with the rest of their wealth; if the Bank *were* wound up, most of them would hardly in their income feel the difference. And what is more, the Bank directors are not trained bankers; they were not bred to the trade, and do not in general give the main power of their minds to it: they are merchants, most of whose time and most of whose real mind are occupied in making money in their own business and for themselves.

It might be expected that as this great public duty was cast upon the Banking Department of the Bank, the principal statesmen (if not Parliament itself) would have enjoined on them to perform it. But no distinct resolution of Parliament has ever enjoined it, scarcely any stray word of any influential statesman: and on the contrary there is a whole *catena* of authorities, beginning with Sir Robert Peel and ending with Mr. Lowe, which say that the Banking Department of the Bank of England is only a bank like any other bank, a company like other companies; that in this capacity it has no peculiar position, and no public duties at all. Nine-tenths of English statesmen, if they were asked as to the management of the Banking Department of the Bank of England, would reply that it was no business of theirs or of Parliament at all; that the Banking Department alone must look to it.

The result is, that we have placed the exclusive custody of our entire banking reserve in the hands

of a single board of directors not particularly trained for the duty, — who might be called "amateurs"; who have no particular interest above other people in keeping it undiminished, who acknowledge no obligation to keep it undiminished, who have never been told by any great statesman or public authority that they are so to keep it or that they have anything to do with it; who are named by and are agents for a proprietary which would have a greater income if it *was* diminished; who do not fear and who need not fear ruin, even if it were all gone and wasted.

That such an arrangement is strange must be plain; but its strangeness can only be comprehended when we know what the custody of a national banking reserve means, and how delicate and difficult it is.

II.

Such a reserve as we have seen is kept to meet sudden and unexpected demands; if the bankers of a country are asked for much more than is commonly wanted, then this reserve must be resorted to. What then are these extra demands? and how is this extra reserve to be used? Speaking broadly, these extra demands are of two kinds: one from abroad to meet foreign payments requisite to pay large and unusual foreign debts, and the other from at home to meet sudden apprehension or panic arising in any manner, rational or irrational.

No country has ever been so exposed as England to a foreign demand on its banking reserve; not only because at present England is a large borrower from foreign nations, but also (and much more) because no nation has ever had a foreign trade of such magnitude, in such varied objects, or so ramified through the world. The ordinary foreign trade of a country requires no cash, — the exports on one side balance the imports on the other; but a sudden trade of import, like the import of foreign corn after a bad

harvest, or (what is much less common, though there are cases of it) the cessation of any great export, causes a balance to become due, which must be paid in cash.

Now, the only source from which large sums of cash can be withdrawn, in countries where banking is at all developed, is a "bank reserve." In England especially, except a few sums of no very considerable amount held by bullion dealers in the course of their business, there are no sums worth mentioning in cash out of the banks; an ordinary person could hardly pay a serious sum without going to some bank, even if he spent a month in trying; all persons who wish to pay a large sum in cash trench of necessity on the banking reserve. But then what is "cash"? Within a country the action of a government can settle the quantity, and therefore the value, of its currency; but outside its own country, no government can do so. Bullion is the "cash" of international trade; paper currencies are of no use there, and coins pass only as they contain more or less bullion.

When then the legal tender of a country is purely metallic, all that is necessary is, that banks should keep a sufficient store of that "legal tender"; but when the "legal tender" is partly metal and partly paper, it is necessary that the paper "legal tender"—the bank note—should be convertible into bullion. And here I should pass my limits and enter on the theory of Peel's Act if I began to discuss the conditions of convertibility. I deal only with the primary prerequisite of effectual foreign payments,—a sufficient supply of the local legal tender; with the after-step—the change of the local legal tender into the universally acceptable commodity—I cannot deal.

What I have to deal with is, for the present, ample enough. The Bank of England must keep a reserve of "legal tender," to be used for foreign payments if itself fit, and to be used in obtaining bullion if itself unfit. And foreign payments are sometimes very

large, and often very sudden: the "cotton drain," as it is called, — the drain to the East to pay for Indian cotton during the American civil war, — took many millions from this country for a series of years; a bad harvest must take millions in a single year. In order to find such great sums, the Bank of England requires the steady use of an effectual instrument.

That instrument is the elevation of the rate of interest. If the interest of money be raised, it is proved by experience that money *does* come to Lombard Street, and theory shows that it *ought* to come. To fully explain the matter I must go deep into the theory of the exchanges, but the general notion is plain enough: loanable capital, like every other commodity, comes where there is most to be made of it. Continental bankers and others instantly send great sums here, as soon as the rate of interest shows that it can be done profitably. While English credit is good, a rise of the value of money in Lombard Street immediately by a banking operation brings money to Lombard Street. And there is also a slower mercantile operation: the rise in the rate of discount acts immediately on the trade of this country. Prices fall here; in consequence imports are diminished, exports are increased, and therefore there is more likelihood of a balance in bullion coming to this country after the rise in the rate than there was before.

Whatever persons — one bank or many banks — in any country hold the banking reserve of that country ought at the very beginning of an unfavorable foreign exchange at once to raise the rate of interest, so as to prevent their reserve from being diminished further, and so as to replenish it by imports of bullion.

This duty, up to about the year 1860, the Bank of England did not perform at all, as I shall show farther on. A more miserable history can hardly be found than that of the attempts of the Bank — if indeed they can be called attempts — to keep a

reserve and to manage a foreign drain between the year 1819 (when cash payments were resumed by the Bank, and when our modern money market may be said to begin) and the year 1857; the panic of that year for the first time taught the Bank directors wisdom, and converted them to sound principles. The present policy of the Bank is an infinite improvement on the policy before 1857; the two must not be for an instant confounded: but nevertheless, as I shall hereafter show, the present policy is now still most defective, and much discussion and much effort will be wanted before that policy becomes what it ought to be.

A domestic drain is very different. Such a drain arises from a disturbance of credit within the country, and the difficulty of dealing with it is the greater because it is often caused, or at least often enhanced, by a foreign drain. Times without number the public have been alarmed mainly because they saw that the banking reserve was already low, and that it was daily getting lower. The two maladies — an external drain and an internal — often attack the money market at once: what then ought to be done?

In opposition to what might be at first sight supposed, the best way for the bank or banks which have the custody of the bank reserve to deal with a drain arising from internal discredit, is to lend freely. The first instinct of every one is the contrary; there being a large demand on a fund which you want to preserve, the most obvious way to preserve it is to hoard it, — to get in as much as you can, and to let nothing go out which you can help: but every banker knows that this is not the way to diminish discredit. This discredit means "an opinion that you have not got any money," and to dissipate that opinion you must if possible show that you have money; you must employ it for the public benefit in order that the public may know that you have it. The time for economy and for accumulation is before:

a good banker will have accumulated in ordinary times the reserve he is to make use of in extraordinary times.

Ordinarily, discredit does not at first settle on any particular bank; still less does it at first concentrate itself on the bank or banks holding the principal cash reserve. These banks are almost sure to be those in best credit, or they would not be in that position; and having the reserve, they are likely to look stronger and seem stronger than any others. At first, incipient panic amounts to a kind of vague conversation: Is A B as good as he used to be? Has not C D lost money? and a thousand such questions. A hundred people are talked about, and a thousand think, "Am I talked about, or am I not?" "Is my credit as good as it used to be, or is it less?" And every day, as a panic grows, this floating suspicion becomes both more intense and more diffused; it attacks more persons, and attacks them all more virulently than at first. All men of experience, therefore, try to "strengthen themselves," as it is called, in the early stage of a panic, — they borrow money while they can: they come to their banker and offer bills for discount which commonly they would not have offered for days or weeks to come; and if the merchant be a regular customer, a banker does not like to refuse, — because if he does he will be said or may be said to be in want of money, and so may attract the panic to himself. Not only merchants, but all persons under pecuniary liabilities, present or imminent, feel this wish to "strengthen themselves," and in proportion to those liabilities. Especially is this the case with what may be called the "auxiliary" dealers in credit. Under any system of banking there will always group themselves about the main bank or banks (in which is kept the reserve) a crowd of smaller money dealers, who watch the minutiæ of bills, look into special securities which busy bankers have not time for, and so gain a livelihood. As

business grows, the number of such subsidiary persons augments: the various modes in which money may be lent have each their peculiarities, and persons who devote themselves to one only lend in that way more safely, and therefore more cheaply. In time of panic these subordinate dealers in money will always come to the principal dealers. In ordinary times the intercourse between the two is probably close enough: the little dealer is probably in the habit of pledging his "securities" to the larger dealer at a rate less than he has himself charged, and of running into the market to lend again; his time and brains are his principal capital, and he wants to be always using them. But in times of incipient panic, the minor money dealer always becomes alarmed: his credit is never very established or very wide; he always fears that he may be the person on whom current suspicion will fasten, and often he is so: accordingly he asks the larger dealer for advances. A number of such persons ask all the large dealers, — those who have the money, the holders of the reserve; and then the plain problem before the great dealers comes to be, "How shall we best protect ourselves? No doubt the immediate advance to these second-class dealers is annoying, but may not the refusal of it even be dangerous? A panic grows by what it feeds on: if it devours these second-class men, shall we, the first-class, be safe?"

A panic, in a word, is a species of neuralgia; and according to the rules of science, you must not starve it. The holders of the cash reserve must be ready not only to keep it for their own liabilities, but to advance it most freely for the liabilities of others; they must lend to merchants, to minor bankers, to "this man and that man," whenever the security is good: in wild periods of alarm, one failure makes many, and the best way to prevent the derivative failures is to arrest the primary failure which causes them. The way in which the panic of 1825 was

stopped by advancing money has been described in so broad and graphic a way that the passage has become classical: —

"We lent it," said Mr. Harman, on behalf of the Bank of England, "by every possible means, and in modes we had never adopted before: we took in stock on security, we purchased Exchequer bills, we made advances on Exchequer bills; we not only discounted outright, but we made advances on the deposit of bills of exchange to an immense amount, — in short, by every possible means consistent with the safety of the Bank, and we were not on some occasions over-nice. Seeing the dreadful state in which the public were, we rendered every assistance in our power."

After a day or two of this treatment, the entire panic subsided, and the "City" was quite calm.

The problem of managing a panic must not be thought of as mainly a "banking" problem: it is primarily a mercantile one. All merchants are under liabilities; they have bills to meet soon, and they can only pay those bills by discounting bills on other merchants. In other words, all merchants are dependent on borrowing money, and large merchants are dependent on borrowing much money. At the slightest symptom of panic, many merchants want to borrow more than usual: they think they will supply themselves with the means of meeting their bills while those means are still forthcoming. If the bankers gratify the merchants, they must lend largely just when they like it least; if they do not gratify them, there is a panic.

On the surface there seems a great inconsistency in all this. First you establish in some bank or banks a certain reserve; you make of it or them a kind of ultimate treasury, where the last shilling of the country is deposited and kept: and then you go on to say that this final treasury is also to be the last lending-house; that out of it unbounded, or at any rate immense advances are to be made when no one else lends. This seems like saying, first that the reserve should be kept, and then that it should not

be kept. But there is no puzzle in the matter: the ultimate banking reserve of a country (by whomsoever kept) is not kept out of show, but for certain essential purposes; and one of those purposes is the meeting a demand for cash caused by an alarm within the country. It is not unreasonable that our ultimate treasure in particular cases should be lent; on the contrary, we keep that treasure for the very reason that in particular cases it should be lent.

When reduced to abstract principle, the subject comes to this:—An "alarm" is an opinion that the money of certain persons will not pay their creditors when those creditors want to be paid; if possible, that alarm is best met by enabling those persons to pay their creditors to the very moment. For this purpose, only a little money is wanted. If that alarm is not so met, it aggravates into a panic, which is an opinion that most people or very many people will not pay their creditors; and this too can only be met by enabling all those persons to pay what they owe, which takes a great deal of money. No one has enough money, or anything like enough, but the holders of the bank reserve.

Not that the help so given by the banks holding that reserve necessarily diminishes it: very commonly the panic extends as far or almost as far as the bank or banks which hold the reserve, but does not touch it or them at all; in this case it is enough if the dominant bank or banks, so to speak, pledge their credit for those who want it. Under our present system, it is often quite enough that a merchant or a banker gets the advance made to him put to his credit in the books of the Bank of England: he may never draw a check on it; or if he does, that check may come in again to the credit of some other customer, who lets it remain on his account. An increase of loans at such times is often an increase of the liabilities of the Bank, not a diminution of its reserve. Just so before 1844, an issue of notes

as in 1825, to quell a panic entirely internal, did not diminish the bullion reserve: the notes went out, but they did not return; they were issued as loans to the public, but the public wanted no more, they never presented them for payment, they never asked that sovereigns should be given for them. But the acceptance of a great liability during an augmenting alarm, though not as bad as an equal advance of cash, is the thing next worse: at any moment the cash *may* be demanded; supposing the panic to grow, it *will* be demanded, and the reserve will be lessened accordingly.

No doubt all precautions may in the end be unavailing. "On extraordinary occasions," says Ricardo, "a general panic seizes the country, when every one is desirous of possessing the precious metals as the most convenient mode of realizing or concealing his property; against such panics, banks have no security *on any system*." * The bank or banks which hold the reserve may last a little longer than the others; but if apprehension pass a certain bound, they must perish too. The use of credit is, that it enables debtors to use a certain part of the money their creditors have lent them. If all those creditors demand all that money at once, they cannot have it; for that which their debtors have used is for the time employed, and not to be obtained. With the advantages of credit we must take the disadvantages too; but to lessen them as much as we can, we must keep a great store of ready money always available, and advance out of it very freely in periods of panic and in times of incipient alarm.

The management of the money market is the more difficult because, as has been said, periods of internal panic and external demand for bullion commonly occur together. The foreign drain empties the Bank till; and that emptiness, and the resulting rise in the

* "Proposals for an Economical and Secure Currency" (MacCulloch's Ricardo, page 406), — slightly rewritten.

rate of discount, tend to frighten the market. The holders of the reserve have therefore to treat two opposite maladies at once: one requiring stringent remedies, and especially a rapid rise in the rate of interest; and the other an alleviative treatment with large and ready loans.

Before we had much specific experience, it was not easy to prescribe for this compound disease; but now we know how to deal with it. We must look first to the foreign drain, and raise the rate of interest as high as may be necessary: unless you can stop the foreign export, you cannot allay the domestic alarm; the Bank will get poorer and poorer, and its poverty will protract or renew the apprehension. And at the rate of interest so raised, the holders — one or more — of the final bank reserve must lend freely. Very large loans at very high rates are the best remedy for the worst malady of the money market, when a foreign drain is added to a domestic drain; any notion that money is not to be had, or that it may not be had at any price, only raises alarm to panic and enhances panic to madness. But though the rule is clear, the greatest delicacy, the finest and best skilled judgment, are needed to deal at once with such great and contrary evils.

And great as is the delicacy of such a problem in all countries, it is far greater in England now than it [ever] was or is elsewhere. The strain thrown by a panic on the final bank reserve is proportional to the magnitude of a country's commerce, and to the number and size of the dependent banks — banks, that is holding no cash reserve — that are grouped around the central bank or banks; and in both respects our system causes a stupendous strain. The magnitude of our commerce, and the number and magnitude of the banks which depend on the Bank of England, are undeniable: there are very many more persons under great liabilities than there are, or ever were, anywhere else. At the commencement of every

panic, all persons under such liabilities try to supply themselves with the means of meeting those liabilities while they can: this causes a great demand for new loans; and so far from being able to meet it, the bankers who do not keep an extra reserve at that time borrow largely, or do not renew large loans, — very likely do both.

London bankers, other than the Bank of England, effect this in several ways. First, they have probably discounted bills to a large amount for the bill-brokers; and if these bills are paid, they decline discounting any others to replace them. The directors of the London and Westminster Bank had, in the panic of 1857, discounted millions of such bills; and they justly said that if those bills were paid, they would have an amount of cash far more than sufficient for any demand.* But how were those bills to be paid? Some one else must lend the money to pay them. The mercantile community could not on a sudden bear to lose so large a sum of borrowed money, — they have been used to rely on it, and they could not carry on their business without it; least of all could they bear it at the beginning of a panic, when everybody wants more money than usual. Speaking broadly, those bills can only be paid by the discount of other bills. When the bills (suppose) of a Manchester warehouseman which he gave to the manufacturer become due, he cannot, as a rule, pay for them at once in cash: he has bought on credit and he has sold on credit, — he is but a middle-man. To pay his own bill to the maker of the goods, he must discount the bills he has received from the shop-keepers to whom he has sold the goods; but if there is a sudden cessation in the means of discount, he will not be able to discount them. All our mercantile community must obtain new loans to pay old debts. If some one else did not pour into the market the money which the banks like the London and

* See Note B in Appendix.

Westminster Bank take out of it, the bills held by the London and Westminster Bank could not be paid.

Who then is to pour in the new money? Certainly not the bill-brokers: they have been used to rediscount with such banks as the London and Westminster millions of bills; and if they see that they are not likely to be able to rediscount those bills, they instantly protect themselves and do not discount them. Their business does not allow them to keep much cash unemployed: they give interest for all the money deposited with them, an interest often nearly approaching the interest they can charge; as they can only keep a small reserve, a panic tells on them more quickly than on any one else. They stop their discounts, or much diminish their discounts, immediately; there is no new money to be had from them, and the only place at which they can have it is the Bank of England.

There is even a simpler case: the banker who is uncertain of his credit, and wants to increase his cash, may have money on deposit at the bill-brokers. If he wants to replenish his reserve, he may ask for it, suppose, just when the alarm is beginning; but if a great number of persons do this very suddenly, the bill-brokers will not at once be able to pay without borrowing. They have excellent bills in their case, but these will not be due for some days; and the demand from the more or less alarmed bankers is for payment at once and to-day. Accordingly the bill-broker takes refuge at the Bank of England, the only place where at such a moment new money is to be had.

The case is just the same if the banker wants to sell consols, or to call in money lent on consols. These he reckons as part of his reserve; and in ordinary times nothing can be better, — according to the saying, you "can sell consols on a Sunday." In a time of no alarm, or in any alarm affecting that particular banker only, he can rely on such reserve

without misgiving: but not so in a general panic, — then, if he wants to sell £500,000 worth of consols, he will not find £500,000 of fresh money ready to come into the market; all ordinary bankers are wanting to sell, or thinking they may have to sell. The only resource is the Bank of England; in a great panic, consols cannot be sold unless the Bank of England will advance to the buyer, and no buyer can obtain advances on consols at such a time unless the Bank of England will lend to him.

The case is worse if the alarm is not confined to the great towns, but is diffused through the country. As a rule, country bankers only keep so much barren cash as is necessary for their common business; all the rest they leave at the bill-brokers or at the interest-giving banks, or invest in consols and such securities. But in a panic they come to London and want this money; and it is only from the Bank of England that they can get it, for all the rest of London want their money for themselves. If we remember that the liabilities of Lombard Street payable on demand are far larger than those of any like market, and that the liabilities of the country are greater still, we can conceive the magnitude of the pressure on the Bank of England when both Lombard Street and the country suddenly and at once come upon it for aid. No other bank was ever exposed to a demand so formidable, for none ever before kept the banking reserve for such a nation as the English.

The mode in which the Bank of England meets this great responsibility is very curious. It unquestionably does make enormous advances in every panic: —

	£		£
In 1847 the loans on "private securities" increased from	18,963,000	to	20,409,000
In 1857 such loans increased from	20,404,000	to	31,350,000
In 1866 such loans increased from	18,507,000	to	33,447,000

But on the other hand, as we have seen, though the Bank more or less does its duty, it does not distinctly acknowledge that it is its duty: we are apt to be

solemnly told that the Banking Department of the Bank of England is only a bank like other banks; that it has no peculiar duty in times of panic; that it then is to look to itself alone, as other banks look. And there is this excuse for the Bank: hitherto questions of banking have been so little discussed in comparison with questions of currency, that the duty of the Bank in time of panic has been put on a wrong ground.

It is imagined that because Bank notes are a legal tender, the Bank has some peculiar duty to help other people; but bank notes are only a legal tender at the Issue Department, not at the Banking Department, and the accidental combination of the two departments in the same building gives the Banking Department no aid in meeting a panic. If the Issue Department were at Somerset House, and if it issued government notes there, the position of the Banking Department under the present law would be exactly what it is now. No doubt, formerly the Bank of England could issue what it pleased; but that historical reminiscence makes it no stronger now that it can no longer so issue, — we must deal with what is, not with what was.

And a still worse argument is also used: it is said that because the Bank of England keeps the "state account" and is the government banker, it is a sort of "public institution" and ought to help everybody. But the custody of the taxes which have been collected and which wait to be expended is a duty quite apart from panics. The government money may chance to be much or little when the panic comes, — there is no relation or connection between the two; and the state, in getting the Bank to keep what money it may chance to have, or in borrowing of it what money it may chance to want, does not hire it to stop a panic or much help it if it tries.

The real reason has not been distinctly seen: as has been already said, — but on account of its importance

and perhaps its novelty it is worth saying again, — whatever bank or banks keep the ultimate banking reserve of the country must lend that reserve most freely in time of apprehension; for that is one of the characteristic uses of the bank reserve, and the mode in which it attains one of the main ends for which it is kept. Whether rightly or wrongly, at present and in fact the Bank of England keeps our ultimate bank reserve, and therefore it must use it in this manner.

And though the Bank of England certainly do make great advances in time of panic, yet as they do not do so on any distinct principle, they naturally do it hesitatingly, reluctantly, and with misgiving. In 1847, even in 1866, — the latest panic, and the one in which on the whole the Bank acted the best, — there was nevertheless an instant when it was believed the Bank would not advance on consols, or at least hesitated to advance on them: the moment this was reported in the City and telegraphed to the country, it made the panic indefinitely worse. In fact, to make large advances in this faltering way is to incur the evil of making them without obtaining the advantage. What is wanted, and what is necessary to stop a panic, is to diffuse the impression that though money may be dear, still money is to be had: if people could be really convinced that they could have money if they wait a day or two, and that utter ruin is not coming, most likely they would cease to run in such a mad way for money. Either shut the Bank at once, and say it will not lend more than it commonly lends, or lend freely, boldly, and so that the public may feel you mean to go on lending. To lend a great deal, and yet not give the public confidence that you will lend sufficiently and effectually, is the worst of all policies; but it is the policy now pursued.

In truth, the Bank do not lend from the motives which should make a bank lend. The holders of the

bank reserve ought to lend at once and most freely in an incipient panic, because they fear destruction in the panic; they ought not to do it to serve others, they ought to do it to serve themselves; they ought to know that this bold policy is the only safe one, and for that reason they ought to choose it. But the Bank directors are not afraid: even at the last moment they say that whatever happens to the community, they can preserve themselves. Both in 1847 and 1857 (I believe also in 1866, though there is no printed evidence of it), the Bank directors contended that the Banking Department was quite safe though its reserve was nearly all gone, and that it could strengthen itself by selling securities and by refusing to discount. But this is a complete dream: the Bank of England could not sell "securities," for in an extreme panic there is no one else to buy securities. The Bank cannot stay still and wait till its bills are paid, and so fill its coffers; for unless it discounts equivalent bills, the bills which it has already discounted will not be paid. When the reserve in the ultimate bank or banks — those keeping the reserve — runs low, it cannot be augmented by the same means that other and dependent banks commonly adopt to maintain their reserve; for the dependent banks trust that at such moments the ultimate banks will be discounting more than usual and lending more than usual, but ultimate banks have no similar rear-guard to rely upon.

I shall have failed in my purpose if I have not proved that the system of intrusting all our reserve to a single board, like that of the Bank directors, is very anomalous; that it is very dangerous; that its bad consequences, though much felt, have not been fully seen, — that they have been obscured by traditional arguments and hidden in the dust of ancient controversies.

But it will be said, What would be better? What other system could there be? We are so accustomed

to a system of banking dependent for its cardinal function on a single bank, that we can hardly conceive of any other; but the natural system — that which would have sprung up if government had let banking alone — is that of many banks of equal or not altogether unequal size. In all other trades, competition brings the traders to a rough approximate equality. In cotton spinning, no single firm far and permanently outstrips the others, — there is no tendency to a monarchy in the cotton world; nor, where banking has been left free, is there any tendency to a monarchy in banking either. In Manchester, in Liverpool, and all through England, we have a great number of banks, each with a business more or less good, but we have no single bank with any sort of predominance; nor is there any such bank in Scotland. In the new world of joint-stock banks outside the Bank of England we see much the same phenomenon: one or more get for a time a better business than the others, but no single bank permanently obtains an unquestioned predominance; none of them gets so much before the others that the others voluntarily place their reserves in its keeping. A republic, with many competitors of a size or sizes suitable to the business, is the constitution of every trade if left to itself, and of banking as much as any other; a monarchy in any trade is a sign of some anomalous advantage, and of some intervention from without.

I shall be at once asked, Do you propose a revolution? Do you propose to abandon the one-reserve system, and create anew a many-reserve system? My plain answer is, that I do not propose it: I know it would be childish. Credit in business is like loyalty in government, — you must take what you can find of it, and work with it if possible. A theorist may easily map out a scheme of government in which Queen Victoria could be dispensed with; he may make a theory that since we admit and we know

that the House of Commons is the real sovereign, any other sovereign is superfluous: but for practical purposes, it is not even worth while to examine these arguments. Queen Victoria is loyally obeyed, without doubt and without reasoning, by millions of human beings: if those millions began to argue, it would not be easy to persuade them to obey Queen Victoria or anything else, — effectual arguments to convince the people who need convincing are wanting. Just so, an immense system of credit, founded on the Bank of England as its pivot and its basis, now exists; the English people, and foreigners too, trust it implicitly. Every banker knows that if he has to *prove* that he is worthy of credit, however good may be his arguments, in fact his credit is gone; but what we have requires no proof, — the whole rests on an instinctive confidence generated by use and years. Nothing would persuade the English people to abolish the Bank of England; and if some calamity swept it away, generations must elapse before at all the same trust would be placed in any other equivalent. A many-reserve system, if some miracle should put it down in Lombard Street, would seem monstrous there; nobody would understand it or confide in it. Credit is a power which may grow, but cannot be constructed; those who live under a great and firm system of credit must consider that if they break up that one they will never see another, for it will take years upon years to make a successor to it.

On this account, I do not suggest that we should return to a natural or many-reserve system of banking; I should only incur useless ridicule if I did suggest it. Nor can I propose that we should adopt the simple and straightforward expedient by which the French have extricated themselves from the same difficulty. In France all banking rests on the Bank of France, even more than in England all rests on the Bank of England, — the Bank of France keeps

the final banking reserve, and it keeps the currency reserve too: but the state does not trust such a function to a board of merchants named by shareholders; the nation itself — the executive government — names the governor and deputy-governor of the Bank of France. These officers have indeed beside them a council of "regents," or directors, named by the shareholders: but they need not attend to that council unless they think fit; they are appointed to watch over the national interest, and in so doing they may disregard the murmurs of the "regents" if they like. And in theory there is much to be said for this plan: the keeping the single banking reserve being a national function, it is at least plausible to argue that government should choose the functionaries. No doubt such a political intervention is contrary to the sound economical doctrine that "banking is a trade, and only a trade": but government forgot that doctrine when, by privileges and monopolies, it made a single bank predominant over all others, and established the one-reserve system; as that system exists, a logical Frenchman consistently enough argues that the state should watch and manage it. But no such plan would answer in England: we have not been trained to care for logical sequence in our institutions, or rather we have been trained not to care for it. And the practical result for which we do care would in this case be bad: the governor of the Bank would be a high parliamentary official, perhaps in the Cabinet, and would change as chance majorities and the strength of parties decide; a trade peculiarly requiring consistency and special attainment would be managed by a shifting and untrained ruler. In fact, the whole plan would seem to an Englishman of business palpably absurd; he would not consider it, he would not think it worth considering. That it works fairly well in France, and that there are specious arguments of theory for it, would not be sufficient to his mind.

All such changes being out of the question, I can propose only three remedies: —

First. There should be a clear understanding between the Bank and the public that since the Bank hold our ultimate banking reserve, they will recognize and act on the obligations which this implies; that they will replenish it in times of foreign demand as fully, and lend it in times of internal panic as freely and readily, as plain principles of banking require.

This looks very different from the French plan, but it is not so different in reality: in England we can often effect by the indirect compulsion of opinion what other countries must effect by the direct compulsion of government; we can do so in this case. The Bank directors now fear public opinion exceedingly; probably no kind of persons are so sensitive to newspaper criticism. And this is very natural. Our statesmen, it is true, are much more blamed, but they have generally served a long apprenticeship to sharp criticism: if they still care for it (and some do, after years of experience, much more than the world thinks), they care less for it than at first, and have come to regard it as an unavoidable and incessant irritant, of which they shall never be rid. But a Bank director undergoes no similar training and hardening. His functions at the Bank fill a very small part of his time; all the rest of his life (unless he be in Parliament) is spent in retired and mercantile industry: he is not subjected to keen and public criticism, and is not taught to bear it. Especially when once in his life he becomes, by rotation, governor, he is most anxious that the two years of office shall "go off well"; he is apt to be irritated even by objections to the principles on which he acts, and cannot bear with equanimity censure which is pointed and personal. At present I am not sure if this sensitiveness is beneficial: as the exact position of the Bank of England in the money market is indistinctly seen, there is no standard to which a

Bank governor can appeal. He is always in fear that "something may be said"; but not quite knowing on what side that "something" may be, his fear is but an indifferent guide to him. But if the cardinal doctrine were accepted, if it were acknowledged that the Bank is charged with the custody of our sole banking reserve and is bound to deal with it according to admitted principles, then a governor of the Bank could look to those principles: he would know which way criticism was coming; if he was guided by the code, he would have a plain defense. And then we may be sure that old men of business would not deviate from the code. At present the Board of Directors are a sort of *semi*-trustees for the nation; I would have them real trustees, and with a good trust deed.

Secondly. The government of the Bank should be improved in a manner to be explained. We should diminish the "amateur" element; we should augment the trained banking element; and we should insure more constancy in the administration.

Thirdly. As these two suggestions are designed to make the Bank as strong as possible, we should look at the rest of our banking system, and try to reduce the demands on the Bank as much as we can. The central machinery being inevitably frail, we should carefully and as much as possible diminish the strain upon it.

But to explain these proposals, and to gain a full understanding of many arguments that have been used, we must look more in detail at the component parts of Lombard Street, and at the curious set of causes which have made it assume its present singular structure.

CHAPTER III.

HOW LOMBARD STREET CAME TO EXIST, AND WHY IT ASSUMED ITS PRESENT FORM.

In the last century, a favorite subject of literary ingenuity was "conjectural history," as it was then called: upon grounds of probability, a fictitious sketch was made of the possible origin of things existing. If this kind of speculation were now applied to banking, the natural and first idea would be that large systems of deposit banking grew up in the early world just as they grow up now in any large English colony. As soon as any such community becomes rich enough to have much money, and compact enough to be able to lodge its money in single banks, it at once begins so to do. English colonists do not like the risk of keeping their money, and they wish to make an interest on it; they carry from home the idea and the habit of banking, and they take to it as soon as they can in their new world. Conjectural history would be inclined to say that all banking began thus; but such history is rarely of any value, — the basis of it is false. It assumes that what works most easily when established is that which it would be the most easy to establish, and that what seems simplest when familiar would be most easily appreciated by the mind though unfamiliar; but exactly the contrary is true, — many things which seem simple, and which work well when firmly established, are very hard to establish among new people and not very easy to explain to them. Deposit banking is of this sort. Its essence is, that a very large number of persons agree to trust a very few persons,

or some one person: banking would not be a profitable trade if bankers were not a small number, and depositors in comparison an immense number. But to get a great number of persons to do exactly the same thing is always very difficult, and nothing but a very palpable necessity will make them on a sudden begin to do it; and there is no such palpable necessity in banking. If you take a country town in France, even now, you will not find any such system of banking as ours: check-books are unknown, and money kept on running account by bankers is rare; people store their money in a *caisse* at their houses. Steady savings, which are waiting for investment and which are sure not to be soon wanted, may be lodged with bankers; but the common floating cash of the community is kept by the community themselves at home, — they prefer to keep it so, and it would not answer a banker's purpose to make expensive arrangements for keeping it otherwise. If a "branch," such as the National Provincial Bank opens in an English country town, were opened in a corresponding French one, it would not pay its expenses: you could not get any sufficient number of Frenchmen to agree to put their money there. And so it is in all countries not of British descent, though in various degrees. Deposit banking is a very difficult thing to begin, because people do not like to let their money out of their sight; especially do not like to let it out of sight without security; still more, cannot all at once agree on any single person to whom they are content to trust it unseen and unsecured. Hypothetical history, which explains the past by what is simplest and commonest in the present, is in banking, as in most things, quite untrue.

The real history is very different. New wants are mostly supplied by adaptation, not by creation or foundation; something having been created to satisfy an extreme want, it is used to satisfy less pressing

wants or to supply additional conveniences. On this account, political government, the oldest institution in the world, has been the hardest worked: at the beginning of history, we find it doing everything which society wants done and forbidding everything which society does *not* wish done. In trade, at present, the first commerce in a new place is a general shop, which, beginning with articles of real necessity, comes shortly to supply the oddest accumulation of petty comforts. And the history of banking has been the same: the first banks were not founded for our system of deposit banking, or for anything like it: they were founded for much more pressing reasons, and having been founded, they or copies from them were applied to our modern uses.

The earliest banks of Italy, where the name began, were finance companies. The Bank of St. George at Genoa, and other banks founded in imitation of it, were at first only companies to make loans to, and float loans for, the governments of the cities in which they were formed. The want of money is an urgent want of governments at most periods, and seldom more urgent than it was in the tumultuous Italian republics of the Middle Ages. After these banks had been long established they began to do what we call "banking" business; but at first they never thought of it. The great banks of the North of Europe had their origin in a want still more curious. The notion of its being a prime business of a bank to give good coin has passed out of men's memories; but wherever it is felt, there is no want of business more keen and urgent. Adam Smith describes it so admirably that it would be stupid not to quote his words: —

"The currency of a great state, such as France or England, generally consists almost entirely of its own coin; should this currency, therefore, be at any time worn, clipped, or otherwise degraded below its standard value, the state by a reformation of its coin can effectually re-establish its currency. But the currency of

a small state, such as Genoa or Hamburg, can seldom consist altogether in its own coin, but must be made up in a great measure of the coins of all the neighboring states with which its inhabitants have a continual intercourse; such a state, therefore, by reforming its coin, will not always be able to reform its currency. If foreign bills of exchange are paid in this currency, the uncertain value of any sum, of what is in its own nature so uncertain, must render the exchange always very much against such a state; its currency being, in all foreign states, necessarily valued even below what it is worth.

"In order to remedy the inconvenience to which this disadvantageous exchange must have subjected their merchants, such small states, when they began to attend to the interest of trade, have frequently enacted that foreign bills of exchange of a certain value should be paid, not in common currency, but by an order upon or by a transfer in the books of a certain bank, established upon the credit and under the protection of the state; this bank being always obliged to pay in good and true money, exactly according to the standard of the state. The banks of Venice, Genoa, Amsterdam, Hamburg, and Nüremberg seem to have been all originally established with this view, though some of them may have afterwards been made subservient to other purposes. The money of such banks, being better than the common currency of the country, necessarily bore an *agio*, which was greater or smaller according as the currency was supposed to be more or less degraded below the standard of the state. The *agio* of the bank of Hamburg, for example, which is said to be commonly about 14 per cent., is the supposed difference between the good standard money of the state and the clipped, worn, and diminished currency poured into it from all the neighboring states.

"Before 1609, the great quantity of clipped and worn foreign coin which the extensive trade of Amsterdam brought from all parts of Europe reduced the value of its currency about 9 per cent. below that of good money fresh from the mint. Such money no sooner appeared than it was melted down or carried away, as it always is in such circumstances: the merchants, with plenty of currency, could not always find a sufficient quantity of good money to pay their bills of exchange; and the value of those bills, in spite of several regulations which were made to prevent it, became in a great measure uncertain.

"In order to remedy these inconveniences, a bank was established in 1609 under the guarantee of the city. This bank received both foreign coin and the light and worn coin of the country at

its real intrinsic value in the good standard money of the country, deducting only so much as was necessary for defraying the expense of coinage and the other necessary expense of management. For the value which remained after this small deduction was made, it gave a credit in its books; this credit was called 'bank money,' which, as it represented money exactly according to the standard of the mint, was always of the same real value, and intrinsically worth more than current money. It was at the same time enacted that all bills drawn upon or negotiated at Amsterdam, of the value of six hundred guilders and upwards, should be paid in bank money; which at once took away all uncertainty in the value of those bills. Every merchant, in consequence of this regulation, was obliged to keep an account with the bank in order to pay his foreign bills of exchange, which necessarily occasioned a certain demand for bank money."*

Again, a most important function of early banks is one which the present banks retain, though it is subsidiary to their main use; viz., the function of remitting money. A man brings money to the bank to meet a payment which he desires to make at a great distance; and the bank, having a connection with other banks, sends it where it is wanted. As soon as bills of exchange are given upon a large scale, this remittance is a very pressing requirement. Such bills must be made payable at a place convenient to the seller of the goods in payment of which they are given, perhaps at the great town where his warehouse is; but this may be very far from the retail shop of the buyer who bought those goods to sell them again in the country. For these and a multitude of purposes, the instant and regular remittance of money is an early necessity of growing trade; and that remittance it was a first object of early banks to accomplish.

These are all uses other than those of deposit banking, which banks supplied that afterwards became in our English sense deposit banks: by supplying these uses, they gained the credit that afterwards

*"Wealth of Nations," Book iv., Chap. iii., "Digression concerning Banks of Deposit."

enabled them to gain a living as deposit banks; being trusted for one purpose, they came to be trusted for a purpose quite different, — ultimately far more important, though at first less keenly pressing. But these wants only affect a few persons, and therefore bring the bank under the notice of a few only. The real introductory function which deposit banks at first perform is much more popular; and it is only when they can perform this more popular kind of business that deposit banking ever spreads quickly and extensively. This function is the supply of the paper circulation to the country; and it will be observed that I am not about to overstep my limits and discuss this as a question of currency. In what form the best paper currency can be supplied to a country is a question of economical theory with which I do not meddle here: I am only narrating unquestionable history, not dealing with an argument where every step is disputed; and part of this certain history is, that the best way to diffuse banking in a community is to allow the banker to issue bank-notes of small amount that can supersede the metal currency. This amounts to a subsidy to each banker to enable him to keep open a bank till depositors choose to come to it. The country where deposit banking is most diffused is Scotland, and there the original profits were entirely derived from the circulation. The note issue is now a most trifling part of the liabilities of the Scotch banks; but it was once their main stay and source of profit. A curious book lately published has enabled us to follow the course of this in detail. The Bank of Dundee, now amalgamated with the Royal Bank of Scotland, was founded in 1763, and had become before its amalgamation, eight or nine years since, a bank of considerable deposits; but for twenty-five years from its foundation it had no deposits at all, — it subsisted mostly on its note issue, and a little on its remittance business. Only in 1792,

after nearly thirty years, it began to gain deposits; but from that time they augmented very rapidly.* The banking history of England has been the same, though we have no country bank accounts in detail which go back so far: but probably up to 1830 in England, or thereabouts, the main profit of banks was derived from the circulation; and for many years after that the deposits were treated as very minor matters, and the whole of so-called banking discussion turned on questions of circulation. We are still living in the *débris* of that controversy; for as I have so often said, people can hardly think of the structure of Lombard Street except with reference to the paper currency, and to the Act of 1844 which regulates it now. The French are still in the same epoch of the subject: their great *enquête* of 1865 is almost wholly taken up with currency matters, and mere banking is treated as subordinate. And the accounts of the Bank of France show why: the last weekly statement before the German war showed that the circulation of the Bank of France was as much as £59,244,000, and that the private deposits were only £17,127,000; now the private deposits are about the same, and the circulation is £112,000,000. So difficult is it in even a great country like France for the deposit system of banking to take root, and establish itself with the strength and vigor that it has in England.

The experience of Germany is the same. The accounts preceding the war in North Germany showed the circulation of the issuing banks to be £39,875,000, and the deposits to be £6,472,000; while the corresponding figures at the present moment are, circulation £60,000,000, and deposits £8,000,000. It would be idle to multiply instances.

The reason why the use of bank paper commonly precedes the habit of making deposits in banks is very plain: it is a far easier habit to establish. In

*See Note C in Appendix.

the issue of notes the banker, the person to be most benefited, can do something, — he can pay away his own "promises" in loans, in wages, or in payment of debts, — but in the getting of deposits he is passive; his issues depend on himself, his deposits on the favor of others. And to the public the change is far easier too: to collect a great mass of deposits with the same banker, a great number of persons must agree to do something; but to establish a note circulation, a large number of persons need only *do nothing*, — they receive the banker's notes in the common course of their business, and they have only *not* to take those notes to the banker for payment. If the public refrain from taking trouble, a paper circulation is immediately in existence. A paper circulation is begun by the banker, and requires no effort on the part of the public, — on the contrary, it needs an effort of the public to be rid of notes once issued; but deposit banking cannot be begun by the banker, and requires a spontaneous and consistent effort in the community: and therefore paper issue is the natural prelude to deposit banking.

The way in which the issue of notes by a banker prepares the way for the deposit of money with him is very plain. When a private person begins to possess a great heap of bank notes, it will soon strike him that he is trusting the banker very much, and that in return he is getting nothing. He runs the risk of loss and robbery just as if he were hoarding coin; he would run no more risk by the failure of the bank if he made a deposit there, and he would be free from the risk of keeping the cash. No doubt it takes time before even this simple reasoning is understood by uneducated minds. So strong is the wish of most people to *see* their money that they for some time continue to hoard bank notes; for a long period a few do so: but in the end common-sense conquers, — the circulation of bank notes decreases and the deposit of money with the banker increases. The

credit of the banker having been efficiently advertised by the note, and accepted by the public, he lives on the credit so gained years after the note issue itself has ceased to be very important to him.

The efficiency of this introduction is proportional to the diffusion of the right of note issue. A single monopolist issuer, like the Bank of France, works its way with difficulty through a country, and advertises banking very slowly; even now the Bank of France, which, I believe, by law ought to have a branch in each Department, has only branches in sixty out of eighty-six. On the other hand, the Swiss banks, where there is always one or more to every Canton, diffuse banking rapidly. We have seen that the liabilities of the Bank of France stand thus:—

	£
Notes, ...	112,000,000
Deposits, ...	15,000,000

But the aggregate Swiss banks, on the contrary, stand:—

	£
Notes, ...	761,000
Deposits, ...	4,709,000*

The reason is, that a central bank, which is governed in the capital and descends on a country district, has much fewer modes of lending money safely than a bank of which the partners belong to that district and know the men and things in it. A note issue is mainly begun by loans; there are then no deposits to be paid. But the mass of loans in a rural district are of small amount; the bills to be discounted are trifling; the persons borrowing are of small means and only local repute, the value of any property they wish to pledge depends on local changes and local circumstances. A banker who lives in the district, who has always lived there, whose whole

*These are the amounts at Dec. 31, 1865. See "Grundzüge der National-Oekonomie, von Max Wirth," Vol. iii., page 491.

mind is a history of the district and its changes, is easily able to lend money safely there; but a manager deputed by a single central establishment does so with difficulty, — the worst people will come to him and ask for loans, his ignorance is a mark for all the shrewd and crafty people thereabouts. He will have endless difficulties in establishing the circulation of the distant bank, because he has not the local knowledge which alone can teach him how to issue that circulation with safety.

A system of note issues is therefore the best introduction to a large system of deposit banking. As yet, historically, it is the only introduction: no nation as yet has arrived at a great system of deposit banking without going first through the preliminary stage of note issue; and of such note issues the quickest and most efficient in this way is one made by individuals resident in the district and conversant with it.

And this explains why deposit banking is so rare: such a note issue as has been described is possible only in a country exempt from invasion and free from revolution. During an invasion, note-issuing banks must stop payment; a run is nearly inevitable at such a time, and in a revolution too. In such great and close civil dangers a nation is always demoralized. Every one looks to himself, and every one likes to possess himself of the precious metals: these are sure to be valuable, invasion or no invasion, revolution or no revolution; but the goodness of bank notes depends on the solvency of the banker, and that solvency may be impaired if the invasion is not repelled or the revolution resisted.

Hardly any Continental country has been till now exempt for long periods *both* from invasion and revolution. In Holland and Germany, — two countries where note issue and deposit banking would seem as natural as in England and Scotland, — there was never any security from foreign war; a profound apprehension of external invasion penetrated their whole habits,

and men of business would have thought it insane not to contemplate a contingency so frequent in their history, and perhaps witnessed by themselves.

France indeed, before 1789, was an exception: for many years under the old *régime* she was exempt from serious invasion or attempted revolution. Her government was fixed, as was then thought, and powerful; it could resist any external enemy, and the *prestige* on which it rested seemed too firm to fear any enemy from within. But then it was not an honest government, and it had shown its dishonesty in this particular matter of note issue: the regent in Law's time had given a monopoly of note issue to a bad bank, and had paid off the debts of the nation in worthless paper; the government had created a machinery of ruin, and had thriven on it. Among so apprehensive a race as the French the result was fatal: for many years no attempt at note issue or deposit banking was possible in France. So late as the foundation of the "Caisse d'Escompte," in Turgot's time, the remembrance of Law's failure was distinctly felt, and impeded the commencement of better attempts.

This therefore is the reason why Lombard Street exists; that is, why England is a very great money market, and other European countries but small ones in comparison. In England and Scotland a diffused system of note issues started banks all over the country; in these banks the savings of the country have been lodged, and by these they have been sent to London. No similar system arose elsewhere; and in consequence London is full of money, and all Continental cities are empty as compared with it.

II.

The monarchical form of Lombard Street is due also to the note issue. The origin of the Bank of England has been told by Macaulay, and it is never wise for an ordinary writer to tell again what he

has told so much better; nor is it necessary, for his writings are in every one's hands: still, I must remind my readers of the curious story.

Of all institutions in the world, the Bank of England is now probably the most remote from party politics and from "financing"; but in its origin it was not only a finance company, but a Whig finance company,—it was founded by a Whig government because it was in desperate want of money, and supported by the "City" because the "City" was Whig. Very briefly, the story was this:—

The government of Charles II. (under the Cabal ministry) had brought the credit of the English state to the lowest possible point: it had perpetrated one of those monstrous frauds which are likewise gross blunders. The goldsmiths, who then carried on upon a trifling scale what we should now call "banking," used to deposit their reserve of treasure in the Exchequer, with the sanction and under the care of the government. In many European countries, the credit of the state had been so much better than any other credit that it had been used to strengthen the beginnings of banking. The credit of the state had been so used in England: though there had lately been a civil war and several revolutions, the honesty of the English government was trusted implicitly. But Charles II. showed that it was trusted undeservedly: he shut up the Exchequer, would pay no one, and so the goldsmiths were ruined.

The credit of the Stuart government never recovered from this monstrous robbery, and the government created by the revolution of 1688 could hardly expect to be more trusted with money than its predecessor. A government created by a revolution hardly ever is: there is a taint of violence which capitalists dread instinctively, and there is always a rational apprehension that the government which one revolution thought fit to set up, another revolution may think fit to pull down. In 1694 the credit of

William III.'s government was so low in London that it was impossible for it to borrow any large sum; and the evil was the greater, because in consequence of the French war the financial straits of the government were extreme. At last a scheme was hit upon which would relieve their necessities. "The plan," says Macaulay, "was, that twelve hundred thousand pounds should be borrowed by the government, on what was then considered as the moderate interest of 8 per cent.* In order to induce capitalists to advance the money promptly on terms so favorable to the public, the subscribers were to be incorporated by the name of 'The Governor and Company of the Bank of England';" they were so incorporated, and the £1,200,000 was obtained.

On many succeeding occasions, their credit was of essential use to the government. Without their aid, our National Debt could not have been borrowed; and if we had not been able to raise that money we should have been conquered by France and compelled to take back James II. And for many years afterwards, the existence of that debt was a main reason why the industrial classes never would think of recalling the Pretender or of upsetting the Revolution settlement: the "fundholder" is always considered in the books of that time as opposed to his "legitimate" sovereign, because it was to be feared that this sovereign would repudiate the debt which was raised by those who dethroned him, and which was spent in resisting him and his allies. For a long time the Bank of England was the focus of London Liberalism, and in that capacity rendered to the state inestimable services; in return for these substantial benefits, the Bank of England received from the government, either at first or afterwards, three most important privileges:—

First. The Bank of England had the exclusive possession of the government balances. In its first

* "History of England," Chap. xx.

period, as I have shown, the Bank gave credit to the government; but afterwards it derived credit from the government. There is a natural tendency in men to follow the example of the government under which they live: the government is the largest, most important, and most conspicuous entity with which the mass of any people are acquainted; its range of knowledge must always be infinitely greater than the average of their knowledge, and therefore, unless there is a conspicuous warning to the contrary, most men are inclined to think their government right, and when they can, to do what it does. Especially in money matters a man might fairly reason, "If the government is right in trusting the Bank of England with the great balance of the nation, I cannot be wrong in trusting it with my little balance."

Second. The Bank of England had till lately the monopoly of limited liability in England. The common law of England knows nothing of any such principle, — it is only possible by royal charter or statute law; and by neither of these was any *real* bank (I do not count absurd schemes such as Chamberlayne's Land Bank*) permitted with limited liability in England till within these few years. Indeed, a good many people thought it was right for the Bank of England, but not right for any other bank. I remember hearing the conversation of a distinguished merchant in the City of London, who well represented the ideas then most current. He was declaiming against banks of limited liability, and some one asked, "Why, what do you say, then, to the Bank of England, where you keep your own account?" "Oh!" he replied, "that is an exceptional case." And no doubt it was an exception of the greatest value to the Bank of England, because it induced many quiet and careful merchants to be

* See Macaulay, "History of England," Chap. xx. The scheme was for the bank to issue notes on landed security to the full value of the land, *and* to rate that value at as many times the annual income as the number of years it was pledged for! — Ed.

directors of the Bank, who certainly would not have joined any bank where *all* their fortunes were liable, and where the liability was not limited.

Thirdly. The Bank of England had the privilege of being the sole *joint-stock company* permitted to issue bank notes in England. Private London bankers did indeed issue notes down to the middle of the last century, but no joint-stock company could do so. The explanatory clause of the Act of 1742 sounds most curiously to our modern ears: —

"And to prevent any doubt that may arise concerning the privilege or power given to the said Governor and Company" — that is, the Bank of England — "of EXCLUSIVE BANKING; and also in regard to creating any other bank or banks by Parliament, or restraining other persons from banking during the continuance of the said privilege granted to the Governor and Company of the Bank of England, as before recited; — it is hereby further enacted and declared by the authority aforesaid, that it is the true intent and meaning of the said act that no other bank shall be created, established, or allowed by Parliament, and that it shall not be lawful for any body politic or corporate whatsoever created or to be created, or for any other persons whatsoever united or to be united in covenants or partnership exceeding the number of six persons in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes payable on demand or at any less time than six months from the borrowing thereof, during the continuance of such said privilege to the said Governor and Company, who are hereby declared to be and remain a corporation with the privilege of exclusive banking, as before recited."

To our modern ears these words seem to mean more than they did. The term "banking" was then applied only to the issue of notes and the taking up of money on bills on demand; our present system of deposit banking, in which no bills or promissory notes are issued, was not then known on a great scale, and was not called "banking." But its effect was very important: it in time gave the Bank of England the monopoly of the note issue of the metropolis. It had at that time no branches, and so it did not compete for the country circulation; but in the metropolis,

where it did compete, it was completely victorious, — no company but the Bank of England could issue notes, and unincorporated individuals gradually gave way and ceased to do so. Up to 1844 London private bankers *might* have issued notes if they pleased; but almost a hundred years ago they were forced out of the field. The Bank of England has so long had a practical monopoly of the circulation that it is commonly believed always to have had a legal monopoly.

And the practical effect of the clause went further: it was believed to make the Bank of England the only joint-stock company that could receive deposits, as well as the only company that could issue notes. The gift of "exclusive banking" to the Bank of England was read in its most natural modern sense: it was thought to prohibit any other banking company from carrying on our present system of banking. After joint-stock banking was permitted in the country, people began to inquire why it should not exist in the metropolis too? and then it was seen that the words I have quoted only forbid the issue of negotiable instruments, and not the receiving of money when no such instrument is given. Upon this construction the London and Westminster Bank and all our older joint-stock banks were founded: but till they began, the Bank of England had among companies not only the exclusive privilege of note issue, but that of deposit banking too; it was in every sense the only *banking* company in London.

With so many advantages over all competitors, it is quite natural that the Bank of England should have far outstripped them all. Inevitably it became *the* bank in London; all the other bankers grouped themselves round it and lodged their reserve with it. Thus our *one*-reserve system of banking was not deliberately founded upon definite reasons; it was the gradual consequence of many singular events, and of an accumulation of legal privileges on a single bank which has now been altered, and which no one would now defend.

CHAPTER IV.

THE POSITION OF THE CHANCELLOR OF THE EXCHEQUER IN THE MONEY MARKET.

NOTHING can be truer in theory than the economical principle that banking is a trade and only a trade; and nothing can be more surely established [or] by a larger experience than that a government which interferes with any trade injures that trade. The best thing, undeniably, that a government can do with the money market is, to let it take care of itself.

But a government can only carry out this principle universally if it observe one condition: it must keep its own money. The government is necessarily at times possessed of large sums in cash. It is by far the richest corporation in the country; its annual revenue payable in money far surpasses that of any other body or person: and if it begins to deposit this immense income, as it accrues, at any bank, at once it becomes interested in the welfare of that bank. It cannot pay the interest on its debt if that bank cannot produce the public deposits when that interest becomes due; it cannot pay its salaries and defray its miscellaneous expenses if that bank fail at any time. A modern government is like a very rich man with very great debts which he cannot well pay: its credit is necessary to its prosperity, almost to its existence; and if its banker fail when one of its debts becomes due, its difficulty is intense.

Another banker, it will be said, may take up the government account; he may advance, as is so often done in other bank failures, what the government

needs for the moment, in order to secure the government account in future: but the imperfection of this remedy is, that it fails in the very worst case, — in a panic, and at a general collapse of credit, no such banker will probably be found. The old banker who possesses the government deposit cannot repay it; and no banker not having that deposit will, at a bad crisis, be able to find the £5,000,000 or £6,000,000 which the quarter-day of a government such as ours requires. If a finance minister, having intrusted his money to a bank, begins to act strictly and say he will in all cases let the money market take care of itself,* the reply is, that in *one* case the money market will take care of *him* too,† and he will be insolvent.

In the infancy of banking, it is probably much better that a government should as a rule keep its own money. If there are not banks in which it can place secure reliance, it should not seem to rely upon them; still less, should it give peculiar favor to any one, and by intrusting it with the government account, secure to it a mischievous supremacy above all other banks. The skill of a financier in such an age is, to equalize the receipt of taxation and the outgoing of expenditure; it should be a principal care with him to make sure that more should not be locked up at a particular moment in the government coffers than is usually locked up there. If the amount of dead capital so buried in the Treasury does not at any time much exceed the common average, the evil so caused is inconsiderable: it is only the loss of interest on a certain sum of money, which would not be much of a burden on the whole nation; the additional taxation it would cause would be inconsiderable. Such an evil is nothing in comparison with that

*Mr. Lowe's famous remark; see Vol. iii., page 433.

†An allusion to Southey's reply to Pitt when told by the latter (in answer to his application for a place for Burns) that "Literature will take care of itself": "Yes, and of you too."—Quoted by Carlyle in "Heroes and Hero Worship," Lecture v.

of losing the money necessary for inevitable expense by intrusting it to a bad bank, or that of recovering this money by identifying the national credit with the bad bank and so propping it up and perpetuating it. So long as the security of the money market is not entirely to be relied on, the government of a country had much better leave it to itself and keep its own money. If the banks are bad, they will certainly continue bad, and will probably become worse, if the government sustains and encourages them. The cardinal maxim is, that any aid to a present bad bank is the surest mode of preventing the establishment of a future good bank.

When the trade of banking began to be better understood, when the banking system was thoroughly secure, the government might begin to lend gradually; especially to lend the unusually large sums which even under the most equable system of finance will at times accumulate in the public exchequer.

Under a natural system of banking it would have every facility. Where there were many banks keeping their own reserve, and each most anxious to keep a sufficient reserve because its own life and credit depended on it, the risk of the government in keeping a banker would be reduced to a minimum; it would have the choice of many bankers, and would not be restricted to any one.

Its course would be very simple, and be analogous to that of other public bodies in the country. The Metropolitan Board of Works, which collects a great revenue in London, has an account at the London and Westminster Bank, for which that bank makes a deposit of consols as a security; the Chancellor of the Exchequer would have no difficulty in getting such security either. If, as is likely, his account would be thought to be larger than any single bank ought to be intrusted with, the public deposits might be divided between several; each would give security, and the whole public money would be safe. If at

any time the floating money in the hands of government were exceptionally large, he might require augmented security to be lodged, and he might obtain an interest. He would be a lender of such magnitude and so much influence that he might command his own terms; he might get his account kept safe if any one could.

If, on the other hand, the Chancellor of the Exchequer were a borrower, as at times he is, he would have every facility in obtaining what he wanted; the credit of the English government is so good that he could borrow better than any one else in the world. He would have greater facility, indeed, than now; for except with the leave of Parliament the Chancellor of the Exchequer cannot borrow by our present laws in the open market, — he can only borrow from the Bank of England, on what are called "deficiency bills." In a natural system he would borrow of any one out of many competing banks, selecting the one that would lend cheapest; but under our present artificial system he is confined to a single bank, which can fix its own charge.

If, contrary to expectation, a collapse occurred, the government might withdraw, as the American government actually has withdrawn, its balance from the bankers;* it might give its aid, lend Exchequer bills, or otherwise pledge its credit for the moment, but when the exigency was passed it might let the offending banks suffer. There would be a penalty for their misconduct; new and better banks, which might take warning from that misconduct, would arise; as in all natural trades, what is old and rotten would perish, what is new and good would replace it: and till the new banks had proved, by good conduct, their fitness for state confidence, the state need not give it.

* It should be remembered, however, that the United States Bank had not "collapsed" and was in no apparent danger when the government ceased depositing new money there, and that the cessation had no connection with business reasons. It never "withdrew its balance" at all. — Ed.

The government could use its favor as a bounty on prudence, and the withdrawal of that favor as a punishment for culpable folly.

Under a good system of banking, a great collapse, except from rebellion or invasion, would probably not happen. A large number of banks, each feeling that their credit was at stake in keeping a good reserve, probably would keep one; if any one did not, it would be criticized constantly, and would soon lose its standing, and in the end disappear. And such banks would meet an incipient panic freely and generously; they would advance out of their reserve boldly and largely, for each individual bank would fear suspicion, and know that at such periods it must "show strength" if at such times it wishes to be thought to have strength. Such a system reduces to a minimum the risk that is caused by the deposit; if the national money can safely be deposited in banks in any way, this is the way to make it safe.

But this system is nearly the opposite to that which the law and circumstances have created for us in England. The English government, far from keeping cash from the money market till the position of that market was reasonably secure, at a very early moment, and while credit of all kinds was most insecure, for its own interests entered into the money market. In order to effect loans better, it gave the custody and profit of its own money (along with other privileges) to a single bank, and therefore practically and in fact it is identified with the Bank to this hour. It cannot let the money market take care of itself, because it has deposited much money in that market, and it cannot pay its way if it loses that money.

Nor would any English statesman propose to "wind up" the Bank of England; a theorist might put such a suggestion on paper, but no responsible Government would think of it. At the worst crisis and in the worst misconduct of the Bank, no such

plea* has been thought of; in 1825 when its till was empty, in 1837 when it had to ask aid from the Bank of France, no such idea was suggested. By irresistible tradition the English government was obliged to deposit its money in the money market, and to deposit with this particular Bank.

And this system has plain and grave evils.

First. Because, being created by state aid, it is more likely than a natural system to require state help.

Secondly. Because, being a *one*-reserve system, it reduces the spare cash of the money market to a smaller amount than any other system, and so makes that market more delicate. There being a less hoard to meet liabilities, any error in the management of that reserve has a proportionately greater effect.

Thirdly. Because our *one* reserve is, by the necessity of its nature, given over to *one* board of directors; and we are therefore dependent on the wisdom of that one only, and cannot, as in most trades, strike an average of the wisdom and the folly, the discretion and the indiscretion, of many competitors.

Lastly. Because that board of directors is, like every other board, pressed on by its shareholders to make a high dividend, and therefore to keep a small reserve, whereas the public interest imperatively requires that they shall keep a large one.

These four evils were inseparable from the system; but there is besides an additional and accidental evil. The English government not only created this singular system, but it proceeded to impair it, and demoralize all the public opinion respecting it. For more than a century after its creation (notwithstanding occasional errors), the Bank of England in the main acted with judgment and with caution. Its business was but small as we should now reckon, but for the most part it conducted that business with prudence and discretion. In 1696 it had been involved

* Probably a misprint for "plan." — Ed.

in the most serious difficulties, and had been obliged to refuse to pay some of its notes; for a long period it was in wholesome dread of public opinion, and the necessity of retaining public confidence made it cautious. But the English government removed that necessity: in 1797 Mr. Pitt feared that he might not be able to obtain sufficient specie for foreign payments, in consequence of the low state of the Bank reserve, and he therefore *required* the Bank not to pay in cash; he removed the preservative apprehension which is the best security of all banks.

For this reason, the period under which the Bank of England did not pay gold for its notes — the period from 1797 to 1819 — is always called the period of the Bank *restriction*. As the Bank during that period did not perform, and was not compelled by law to perform, its contract of paying its notes in cash, it might apparently have been well called the period of Bank "license." But the word "restriction" was quite right, and was the only proper word as a description of the policy of 1797: Mr. Pitt did not say that the Bank of England need not pay its notes in specie, — he "restricted" them from doing so; he said that they must not.

In consequence, from 1797 to 1844 (when a new era begins), there never was a proper caution on the part of the Bank directors; at heart they considered that the Bank of England had a kind of charmed life, and that it was above the ordinary banking anxiety to pay its way. And this feeling was very natural: a bank of issue which need not pay its notes in cash *has* a charmed life; it can lend what it wishes and issue what it likes, with no fear of harm to itself and with no substantial check but its own inclination. For nearly a quarter of a century the Bank of England *was* such a bank, for all that time it *could* not be in any danger. And naturally the public mind was demoralized also: since 1797 the public have always expected the government to help the

Bank if necessary. I cannot fully discuss the suspensions of the Act of 1844 in 1847, 1857, and 1866: but indisputably one of their effects is to make people think that government will always help the Bank if the Bank is in extremity; and this is the sort of anticipation which tends to justify itself and to cause what it expects.

On the whole, therefore, the position of the Chancellor of the Exchequer in our money market is that of one who deposits largely in it, who created it, and who demoralized it. He cannot, therefore, banish it from his thoughts or decline responsibility for it: he must arrange his finances so as not to intensify panics, but to mitigate them; he must aid the Bank of England in the discharge of its duties, he must not impede or prevent it.

His aid may be most efficient: he is, on finance, the natural exponent of the public opinion of England; and it is by that opinion that we wish the Bank of England to be guided. Under a natural system of banking we should have relied on self-interest, but the state prevented that: we now rely on opinion instead, — the public approval is a reward, its disapproval a severe penalty, on the Bank directors; and of these it is most important that the finance minister should be a sound and felicitous exponent.

CHAPTER V.

THE MODE IN WHICH THE VALUE OF MONEY IS SETTLED IN LOMBARD STREET.

MANY persons believe that the Bank of England has some peculiar power of fixing the value of money. They see that the Bank of England varies its minimum rate of discount from time to time, and that, more or less, all other banks follow its lead and charge much as it charges; and they are puzzled why this should be. "Money," as economists teach, "is a commodity, and only a commodity:" why then, it is asked, is its value fixed in so odd a way, and not the way in which the value of all other commodities is fixed?

There is at bottom, however, no difficulty in the matter: the value of money is settled, like that of all other commodities, by supply and demand, and only the form is essentially different. In other commodities all the large dealers fix their own price: they try to underbid one another, and that keeps down the price; they try to get as much as they can out of the buyer, and that keeps up the price: between the two, what Adam Smith calls "the higgling of the market"* settles it. And this is the most simple and natural mode of doing business, but it is not the only mode, — if circumstances make it convenient another may be adopted: a single large holder — especially if he be by far the greatest holder — may fix his price, and other dealers may say whether or not they will undersell him, or whether or not they will ask more than he does. A very considerable holder of an

* "Higgling and bargaining of the market." — Book i., Chap. v.

article may, for a time, vitally affect its value, if he lay down the minimum price which he will take and obstinately adhere to it. This is the way in which the value of money in Lombard Street is settled: the Bank of England used to be a predominant, and is still a most important, dealer in money; it lays down the least price at which alone it will dispose of its stock, and this for the most part enables other dealers to obtain that price, or something near it.

The reason is obvious. At all ordinary moments there is not money enough in Lombard Street to discount all the bills in Lombard Street without taking some money from the Bank of England. As soon as the Bank rate is fixed, a great many persons who have bills to discount, try how much cheaper than the Bank they can get these bills discounted; but they seldom can get them discounted very much cheaper, for if they did every one would leave the Bank, and the outer market would have more bills than it could bear.

In practice, when the Bank finds this process beginning, and sees that its business is much diminishing, it lowers the rate, so as to secure a reasonable portion of the business to itself and to keep a fair part of its deposits employed. At Dutch auctions an upset or *maximum* price used to be fixed by the seller, and he came down in his bidding till he found a buyer; the value of money is fixed in Lombard Street in much the same way, only that the upset price is not that of all sellers, but that of one very important seller, some part of whose supply is essential.

The notion that the Bank of England has a control over the money market, and can fix the rate of discount as it likes, has survived from the old days before 1844, when the Bank could issue as many notes as it liked; but even then the notion was a mistake. A bank with a monopoly of note issue has great sudden power in the money market, but no

permanent power; it can affect the rate of discount at any particular moment, but it cannot affect the average rate: and the reason is, that any momentary fall in money, caused by the caprice of such a bank, of itself tends to create an immediate and equal *rise*, so that upon an average the value is not altered.

What happens is this:—If a bank with a monopoly of note issue suddenly lends (suppose) £2,000,000 more than usual, it causes a proportionate increase of trade and increase of prices. The persons to whom that £2,000,000 was lent did not borrow it to lock it up: they borrow it, in the language of the market, to "operate with,"—that is, they try to buy with it; and that new attempt to buy, that new demand, raises prices. And this rise of prices has three consequences:—First, it makes everybody else want to borrow money: money is not so efficient in buying as it was, and therefore operators require more money for the same dealings. If railway stock is 10 per cent. dearer this year than last, a speculator who borrows money to enable him to deal must borrow 10 per cent. more this year than last, and in consequence there is an augmented demand for loans. Secondly, this is an *effectual* demand; for the increased price of railway stock enables those who wish it to borrow more upon it. The common practice is to lend a certain portion of the market value of such securities; and if that value increases, the amount of the usual loan to be obtained on them increases too. In this way, therefore, any artificial reduction in the value of money causes a new augmentation of the demand for money, and thus restores that value to its natural level. In all business this is well known by experience,—a stimulated market soon becomes a tight market; for so sanguine are enterprising men, that as soon as they get any unusual ease they always fancy that the relaxation is greater than it is, and speculate till they want more than they can obtain.

In these two ways, sudden loans by an issuer of notes, though they may temporarily lower the value of money, do not lower it permanently, because they generate their own counteraction; and this they do whether the notes issued are convertible into coin or not, — during the period of Bank restriction, from 1797 to 1819, the Bank of England could not absolutely control the money market any more than it could after 1819, when it was compelled to pay its notes in coin. But in the case of convertible notes there is a *third* effect, which works in the same direction and works more quickly: — A rise of prices confined to one country tends to increase imports, because other countries can obtain more for their goods if they send them there; and it discourages exports, because a merchant who would have gained a profit before the rise by buying [t]here to sell again, will not gain so much if any profit after that rise. By this augmentation of imports the indebtedness of this country is augmented, and by this diminution of exports the proportion of that indebtedness which is paid in the usual way is decreased also. In consequence, there is a larger balance to be paid in bullion; the store in the bank or banks keeping the reserve is diminished, and the rate of interest must be raised by them to stay the efflux: and the tightness so produced is often greater than, and always equal to, the preceding unnatural laxity.

There is therefore no ground for believing, as is so common, that the value of money is settled by different causes than those which affect the value of other commodities, or that the Bank of England has any despotism in that matter; it has the power of a large holder of money, and no more. Even formerly, when its monetary powers were greater and its rivals weaker, it had no absolute control: it was simply a large corporate dealer, making bids and much influencing — though in no sense compelling — other dealers thereby.

But though the value of money is not settled in an exceptional way, there is nevertheless a peculiarity about it, as there is about many articles: it is a commodity subject to great fluctuations of value, and those fluctuations are easily produced by a slight excess or a slight deficiency of quantity. Up to a certain point, money is a necessity: if a merchant has acceptances to meet to-morrow, money he must and will find to-day at some price or other; and it is this urgent need of the whole body of merchants which runs up the value of money so wildly and to such a height in a great panic. On the other hand, money easily becomes a "drug," as the phrase is, and there is soon too much of it: the number of accepted securities is limited, and cannot be rapidly increased; if the amount of money seeking these accepted securities is more than can be lent on them, the value of money soon goes down. You may often hear in the market that bills are not to be had, — meaning good bills, of course; and when you hear this, you may be sure that the value of money is very low.

If money were all held by the owners of it, or by banks which did not pay an interest for it, the value of money might not fall so fast: money would, in the market phrase, be "well held"; the possessors would be under no necessity to employ it all, — they might employ part at a high rate rather than all at a low rate. But in Lombard Street, money is very largely held by those who *do* pay an interest for it, and such persons must employ it all or almost all; for they have much to pay out with one hand, and unless they receive much with the other they will be ruined. Such persons do not so much care what is the rate of interest at which they employ their money, — they can reduce the interest they pay in proportion to that which they can make; the vital point to them is, to employ it at *some* rate. If you hold (as in Lombard Street some persons do) millions of other people's money at interest, arithmetic

teaches that you will soon be ruined if you make nothing of it, even if the interest you pay is not high.'

The fluctuations in the value of money are therefore greater than those on the value of most other commodities: at times there is an excessive pressure to borrow it, and at times an excessive pressure to lend it, and so the price is forced up and down.

These considerations enable us to estimate the responsibility which is thrown on the Bank of England by our system, and by every system on the bank or banks who by it keep the reserve of bullion or of legal tender exchangeable for bullion. These banks can in no degree control the permanent value of money, but they can completely control its momentary value; they cannot change the average value, but they can determine the deviations from the average. If the dominant banks manage ill, the rate of interest will at one time be excessively high, and at another time excessively low; there will be first a pernicious excitement, and next a fatal collapse. But if they manage well, the rate of interest will not deviate so much from the average rate; it will neither ascend so high nor descend so low. As far as anything can be steady, the value of money will then be steady; and probably in consequence trade will be steady too, — at least a principal cause of periodical disturbance will have been withdrawn from it.

CHAPTER VI.

WHY LOMBARD STREET IS OFTEN VERY DULL AND SOMETIMES EXTREMELY EXCITED.

Any sudden event which creates a great demand for actual cash may cause, and will tend to cause, a panic in a country where cash is much economized, and where debts payable on demand are large. In such a country an immense credit rests on a small cash reserve: and an unexpected and large diminution of that reserve may easily break up and shatter very much if not the whole of that credit. Such accidental events are of the most various nature; a bad harvest, an apprehension of foreign invasion, the sudden failure of a great firm which everybody trusted, and many other similar events, have all caused a sudden demand for cash: and some writers have endeavored to classify panics according to the nature of the particular accidents producing them. But little, however, is, I believe, to be gained by such classifications; there is little difference in the effect of one accident and another upon our credit system: we must be prepared for all of them, and we must prepare for all of them in the same way, — by keeping a large cash reserve.

But it is of great importance to point out that our industrial organization is liable not only to irregular external accidents, but likewise to regular internal changes; that these changes make our credit system much more delicate at some times than at others; and that it is the recurrence of these periodical seasons of delicacy which has given rise to the notion

that panics come according to a fixed rule, — that every ten years or so we must have one of them.

Most persons who begin to think of the subject are puzzled on the threshold. They hear much of "good times" and "bad times," meaning by "good" times in which nearly every one is very well off, and by "bad" times in which nearly every one is comparatively ill off. And at first it is natural to ask, Why should everybody, or almost everybody, be well off together? Why should there be any great tides of industry, with large diffused profit by way of flow, and large diffused want of profit, or loss, by way of ebb? The main answer is hardly given distinctly in our common books of political economy; these books do not tell you what is the fund out of which large general profits are paid in good times, nor do they explain why that fund is not available for the same purpose in bad times.

Our current political economy does not sufficiently take account of *time* as an element in trade operations; but as soon as the division of labor has once established itself in a community, two principles at once begin to be important, of which time is the very essence. These are —

First. That as goods are produced to be exchanged, it is good that they should be exchanged as quickly as possible.

Secondly. That as every producer is mainly occupied in producing what others want, and not what he wants himself, it is desirable that he should always be able to find, without effort, without delay, and without uncertainty, others who want what he can produce.

In themselves these principles are self-evident: every one will admit it to be expedient that all goods wanting to be sold should be sold as soon as they are ready; that every man who wants to work should find employment as soon as he is ready for it. Obviously also, as soon as the "division of labor"

is really established, there is a difficulty about both of these principles: A produces what he thinks B wants, but it may be a mistake, and B may not want it; A may be able and willing to produce what B wants, but he may not be able to find B,—he may not know of his existence.

The general truth of these principles is obvious; but what is not obvious is the extreme greatness of their effects. Taken together, they make the whole difference between times of brisk trade and great prosperity and times of stagnant trade and great adversity, so far as that prosperity and that adversity are real and not illusory. If they are satisfied, every one knows whom to work for and what to make, and he can get immediately in exchange what he wants himself; there is no idle labor and no sluggish capital in the whole community: and in consequence all which can be produced is produced, the effectiveness of human industry is augmented, and both kinds of producers—both capitalists and laborers—are much richer than usual, because the amount to be divided between them is also much greater than usual.

And there is a partnership in industries. No single large industry can be depressed without injury to other industries; still less can any great group of industries. Each industry when prosperous buys and consumes the produce probably of most (certainly of very many) other industries: and if industry A fail and is in difficulty, industries B and C and D, which used to sell to it, will not be able to sell that which they had produced in reliance on A's demand; and in future they will stand idle till industry A recovers, because in default of A there will be no one to buy the commodities which they create. Then, as industry B buys of C, D, etc., the adversity of B tells on C, D, etc.; and as these buy of E, F, etc., the effect is propagated through the whole alphabet. And in a certain sense it rebounds: Z feels

the want caused by the diminished custom of A, B, and C, and so it does not earn so much; in consequence it cannot lay out as much on the produce of A, B, and C, and so these do not earn as much either. In all this, money is but an instrument; the same thing would happen equally well in a trade of barter, if a state of barter on a very large scale were not practically impossible on account of the time and trouble which it would necessarily require. As has been explained, the fundamental cause is, that under a system in which every one is dependent on the labor of every one else, the loss of one spreads and multiplies through all; and spreads and multiplies the faster, the higher the previous perfection of the system of divided labor and the more nice and effectual the mode of interchange. And the entire effect of a depression in any single large trade requires a considerable *time* before it can be produced; it has to be propagated and to be returned through a variety of industries, before it is complete. Short depressions, in consequence, have scarcely any discernible consequences; they are over before we think of their effects. It is only in the case of continuous and considerable depressions that the cause is in action long enough to produce discernible effects.

The most common and by far the most important case where the depression in one trade causes depression in all others, is that of depressed agriculture. When the agriculture of the world is ill off, food is dear; and as the amount of absolute necessaries which a people consumes cannot be much diminished, the additional amount which has to be spent on them is so much subtracted from what used to be spent on other things. All the industries, A, B, C, D, up to Z, are somewhat affected by an augmentation in the price of corn; and the most affected are the large ones, which produce the objects in ordinary times most consumed by the working classes. The clothing trades feel the difference at once; and in this country

the liquor trade (a great source of English revenue) feels it almost equally soon. Especially when for two or three years harvests have been bad and corn has long been dear, every industry is impoverished; and almost every one, by becoming poorer, makes every other poorer too. All trades are slack from diminished custom; and the consequence is a vast stagnant capital, much idle labor, and a greatly retarded production.

It takes two or three years to produce this full calamity, and the recovery from it takes two or three years also. If corn should long be cheap, the laboring classes have much to spend on what they like besides: the producers of those things become prosperous, and have a greater purchasing power; they exercise it, and that creates in the class they deal with another purchasing power, and so all through society. The whole machine of industry is stimulated to its maximum of energy, just as before much of it was slackened almost to its minimum.

A great calamity to any great industry will tend to produce the same effect; but the fortunes of the industries on which the wages of labor are expended are much more important than those of all others, because they act much more quickly upon a larger mass of purchasers. On principle, if there were a perfect division of labor, every industry would have to be perfectly prosperous in order that any one might be so. So far, therefore, from its being at all natural that trade should develop constantly, steadily, and equably, it is plain, without going farther, from theory as well as from experience, that there are inevitably periods of rapid dilatation, and as inevitably periods of contraction and of stagnation.

Nor is this the only changeable element in modern industrial societies: credit — the disposition of one man to trust another — is singularly varying. In England, after a great calamity, everybody is suspicious of everybody; as soon as that calamity is forgotten,

everybody again confides in everybody. On the Continent there has been a stiff controversy as to whether credit should or should not be called "capital"; in England even the little attention once paid to abstract economics is now diverted, and no one cares in the least for refined questions of this kind. The material practical point is, that (in M. Chevalier's language) credit is "additive," or additional, — that is, in times when credit is good productive power is more efficient, and in times when credit is bad productive power is less efficient. And the state of credit is thus influential because of the two principles which have just been explained: in a good state of credit, goods lie on hand a much less time than when credit is bad; sales are quicker; intermediate dealers borrow easily to augment their trade, and so more and more goods are more quickly and more easily transmitted from the producer to the consumer.

These two variable causes are causes of real prosperity: they augment trade and production, and so are plainly beneficial, — except where by mistake the wrong things are produced; or where, also by mistake, misplaced credit is given, and a man who cannot produce anything which is wanted gets the produce of other people's labor upon a false idea that he will produce it. But there is another variable cause, which produces far more of apparent than of real prosperity, and of which the effect is in actual life mostly confused with those of the others.

In our common speculations we do not enough remember that interest on money is a refined idea, and not a universal one; so far indeed is it from being universal, that the majority of saving persons in most countries would reject it. Most savings in most countries are held in hoarded specie; in Asia, in Africa, in South America, largely even in Europe, they are thus held, and it would frighten most of the owners to let them out of their keeping. An Englishman — a modern Englishman at least — assumes as a

first principle that he ought to be able to "put his money into something safe that will yield 5 per cent."; but most saving persons in most countries are afraid to "put their money" into anything. Nothing is safe, to their minds; indeed, in most countries, owing to a bad government and a backward industry, no investment, or hardly any, really is safe. In most countries most men are content to forego interest: but in more advanced countries, at some times there are more savings seeking investment than there are known investments for; at other times there is no such superabundance. Lord Macaulay has graphically described one of the periods of excess. He says:—

"During the interval between the Restoration and the Revolution the riches of the nation had been rapidly increasing. Thousands of busy men found every Christmas that after the expenses of the year's housekeeping had been defrayed out of the year's income, a surplus remained; and how that surplus was to be employed was a question of some difficulty. In our time, to invest such a surplus, at something more than three per cent., on the best security that has ever been known in the world, is the work of a few minutes; but in the seventeenth century, a lawyer, a physician, a retired merchant, who had saved some thousands and who wished to place them safely and profitably, was often greatly embarrassed. Three generations earlier, a man who had accumulated wealth in a profession generally purchased real property, or lent his savings on mortgage. But the number of acres in the kingdom had remained the same; and the value of those acres, though it had greatly increased, had by no means increased so fast as the quantity of capital which was seeking for employment. Many too wished to put their money where they could find it at an hour's notice, and looked about for some species of property which could be more readily transferred than a house or a field. A capitalist might lend on bottomry or on personal security; but if he did so, he ran a great risk of losing interest and principal. There were a few joint-stock companies, among which the East India Company held the foremost place; but the demand for the stock of such companies was far greater than the supply. Indeed, the cry for a new East India Company was chiefly raised by persons who had found difficulty in placing their savings at interest on good security. So great was that difficulty that the practice of

hoarding was common. We are told that the father of Pope the poet, who retired from business in the City about the time of the Revolution, carried to a retreat in the country a strong box containing near twenty thousand pounds, and took out from time to time what was required for household expenses;* and it is highly probable that this was not a solitary case. At present the quantity of coin which is hoarded by private persons is so small that it would, if brought forth, make no perceptible addition to the circulation; but in the earlier part of the reign of William III., all the greatest writers on currency were of opinion that a very considerable mass of gold and silver was hidden in secret drawers and behind wainscots.

"The natural effect of this state of things was, that a crowd of projectors, ingenious and absurd, honest and knavish, employed themselves in devising new schemes for the employment of redundant capital. It was about the year 1688 that the word 'stock-jobber' was first heard in London. In the short space of four years a crowd of companies, every one of which confidently held out to subscribers the hope of immense gains, sprang into existence: the Insurance Company, the Paper Company, the Lutestring Company, the Pearl Fishery Company, the Glass Bottle Company, the Alum Company, the Blythe Coal Company, the Swordblade Company. There was a Tapestry Company, which would soon furnish pretty hangings for all the parlors of the middle class and for all the bedchambers of the higher. There was a Copper Company, which proposed to explore the mines of England, and held out a hope that they would prove not less valuable than those of Potosi. There was a Diving Company, which undertook to bring up precious effects from shipwrecked vessels, and which announced that it had laid in a stock of wonderful machines resembling complete suits of armor. In front of the helmet was a huge glass eye like that of a Cyclops; and out of the crest went a pipe through which the air was to be admitted. The whole process was exhibited on the Thames. Fine gentlemen and fine ladies were invited to the show, were hospitably regaled, and were delighted by seeing the divers in their panoply descend into the river and return laden with old iron and ship's tackle. There was a Greenland Fishing Company, which could not fail to drive the Dutch whalers and herring busses out of the Northern Ocean. There was a Tanning Company, which promised to furnish leather superior to the best that was brought from Turkey or Russia. There was a society which undertook the office of giving gentlemen a liberal education on low terms, and which assumed the sounding name of the Royal

* Not a fact. See note to Vol. ii., page 87.

Academies Company. In a pompous advertisement it was announced that the directors of the Royal Academies Company had engaged the best masters in every branch of knowledge, and were about to issue twenty thousand tickets at twenty shillings each. There was to be a lottery, — two thousand prizes were to be drawn; and the fortunate holders of the prizes were to be taught, at the charge of the Company, Latin, Greek, Hebrew, French, Spanish, conic sections, trigonometry, heraldry, japaning, fortification, book-keeping, and the art of playing the theorbo." *

The panic was forgotten till Lord Macaulay revived the memory of it. But in fact, in the South Sea Bubble, which has always been remembered, the form was the same, only a little more extravagant; the companies in that mania were for objects such as these: —

"'Wrecks to be fished for on the Irish Coast — Insurance of Horses, and other Cattle (two millions) — Insurance of Losses by Servants — To make Salt Water Fresh — For building of Hospitals for Bastard Children — For building of Ships against Pirates — For making of Oil from Sun-flower Seeds — For improving of Malt Liquors — For recovering of Seamen's Wages — For extracting of Silver from Lead — For the transmuting of Quicksilver into a malleable and fine Metal — For making of Iron with Pit-coal — For importing a Number of large Jack Asses from Spain — For trading in Human Hair — For fatting of Hogs — For a Wheel for a Perpetual Motion.' But the most strange of all, perhaps, was 'For an Undertaking which shall in due time be revealed.' Each subscriber was to pay down two guineas, and hereafter to receive a share of one hundred, with a disclosure of the object; and so tempting was the offer, that 1,000 of these subscriptions were paid the same morning, with which the projector went off in the afternoon." †

In 1825 there were speculations in companies nearly as wild; and just before 1866 there were some of a like nature, though not equally extravagant. The fact is, that the owners of savings, not finding in adequate quantities their usual kind of investments, rush into anything that promises speciously; and when they find that these specious investments can be disposed of at a high profit, they rush into them

* "History of England," Chap. xix.

† Mahon's "History of England," Chap. xi.

more and more. The first taste is for high interest, but that taste soon becomes secondary; there is a second appetite for large gains to be made by selling the principal which is to yield the interest. So long as such sales can be effected, the mania continues; when it ceases to be possible to effect them, ruin begins.

So long as the savings remain in possession of their owners, these hazardous gamblings in speculative undertakings are almost the whole effect of an excess of accumulation over tested investment; little effect is produced on the general trade of the country, — the owners of the savings are too scattered and far from the market to change the majority of mercantile transactions. But when these savings come to be lodged in the hands of bankers, a much wider result is produced. Bankers are close to mercantile life; they are always ready to lend on good mercantile securities, they wish to lend on such securities a large part of the money intrusted to them. When therefore the money so intrusted is unusually large, and when it long continues so, the general trade of the country is in the course of time changed. Bankers are daily more and more ready to lend money to mercantile men; more is lent to such men; more bargains are made in consequence; commodities are more sought after: and in consequence, prices rise more and more.

The rise of prices is quickest in an improving state of credit. Prices in general are mostly determined by wholesale transactions: the retail dealer adds a percentage to the wholesale prices, — not of course always the same percentage, but still mostly the same; given the wholesale price of most articles, you can commonly tell their retail price. Now, wholesale transactions are commonly not cash transactions, but bill transactions. The duration of the bill varies with the custom of the trade; it may be two, three months, or six weeks, but there is always a bill. Times of credit mean times in which the bills of many people

are taken readily; times of bad credit, times when the bills of much fewer people are taken, and even of those suspiciously. In times of good credit there are a great number of strong purchasers, and in times of bad credit only a smaller number of weak ones; and therefore years of improving credit, if there be no disturbing cause, are years of rising price, and years of decaying credit, years of falling price.

This is the meaning of the saying, "John Bull can stand many things, but he cannot stand two per cent.": it means that the greatest effect of the three great causes is nearly peculiar to England. Here and here almost alone the excess of savings over investments is deposited in banks; here and here only is it made use of so as to affect trade at large; here and here only are prices gravely affected. In these circumstances a low rate of interest, long protracted, is equivalent to a total depreciation of the precious metals. In his book on the effect of the great gold discoveries, Professor Jevons showed — and so far as I know, was the first to show — the necessity of eliminating these temporary changes of value in gold before you could judge properly of the permanent depreciation. He proved that in the years preceding both 1847 and 1857 there was a general rise of prices, and in the years succeeding these years a great fall. The same might be shown of the years before and after 1866, *mutatis mutandis*.

And at the present moment we have a still more remarkable example, which was thus analyzed in the *Economist* of the 30th December, 1871, in an article which I venture to quote as a whole: —

THE GREAT RISE IN THE PRICE OF COMMODITIES.

Most persons are aware that the trade of the country is in a state of great activity. All the usual tests indicate that: the state of the revenue, the bankers' clearing-house figures, the returns of exports and imports, are all plain, and all speak the same language. But few have, we think, considered one most remarkable feature of the present time, or have sufficiently examined its consequences; that feature is the great rise in the price of most of the leading

articles of trade during the past year. We give at the foot of this paper a list of articles comprising most first-rate articles of commerce: and it will be seen that the rise of price, though not universal and not uniform, is nevertheless very striking and very general. The most remarkable cases are —

	January. £	s.	d.	December. £	s.	d.
Wool — South Down hogs, per pack,	13	0	0	21	15	0
Cotton — Upland ordinary, per lb.,	0	0	7¼	0	0	8⅜
No. 40 mule yarn, etc., "	0	1	1½	0	1	2½
Iron — Bars, British, . . per ton,	7	2	6	8	17	6
Pig, No. 1 Clyde, . . "	2	13	3	3	16	0
Lead, ... "	18	7	6	19	2	6
Tin, ... "	137	0	0	157	0	0
Copper — Sheeting, . . "	75	10	0	95	0	0
Wheat (*Gazette* average), per qr.,	2	12	0	2	15	8

and in other cases there is a tendency upwards in price much more often than there is a tendency downwards.

This general rise of price must be due either to a diminution in the supply of the quoted articles, or to an increased demand for them. In some cases there has no doubt been a short supply; thus in wool, the diminution in the home breed of sheep has had a great effect on the price: —

In 1869 the home stock of sheep was . . .	29,538,000
In 1871 " " " . . .	27,133,000
Diminution, ...	2,405,000

Equal to 8.1 per cent.

and in the case of some other articles there may be a similar cause operating. But taking the whole mass of the supply of commodities in this country, as shown by the plain test of the *quantities* imported, it has not diminished, but augmented. The returns of the Board of Trade prove this in the most striking manner, and we give below a table of some of the important articles. The rise in prices must therefore be due to an increased demand; and the first question is, To what is that demand due?

We believe it to be due to the combined operation of three causes: cheap money, cheap corn, and improved credit. As to the first, indeed, it might be said at first sight that so general an increase must be due to a depreciation of the precious metals; certainly, in many controversies, facts far less striking have been alleged as proving it: and indeed there plainly is a diminution in the *purchasing power* of money, though that diminution is not

general and permanent, but local and temporary. The peculiarity of the precious metals is, that their value depends for unusually long periods on the quantity of them which is in the market. In the long run, their value, like that of all others, is determined by the cost at which they can be brought to market; but for all temporary purposes, it is the supply in the market which governs the price, and that supply in this country is exceedingly variable. After a commercial crisis—1866, for example—two things happen:—First, we call in the debts which are owing to us in foreign countries; and we require these debts to be paid to us, not in commodities, but in money. From this cause principally, and omitting minor causes, the bullion in the Bank of England, which was £13,156,000 in May, 1866, rose to £19,413,000 in January, 1867, being an increase of over £6,000,000. And then there comes also a second cause, tending in the same direction. During a depressed period the savings of the country increase considerably faster than the outlet for them; a person who has made savings does not know what to do with them: and this new unemployed saving means additional money. Till a saving is invested or employed, it exists only in the form of money: a farmer who has sold his wheat and has £100 "to the good," holds that £100 in money, or some equivalent for money, till he sees some advantageous use to be made of it. Probably he places it in a bank, and this enables it to do more work: if £3,000,000 of coin be deposited in a bank, and it need only keep £1,000,000 as a reserve, that sets £2,000,000 free, and is for the time equivalent to an increase of so much coin. As a principle, it may be laid down that all new unemployed savings require *either an increased stock of the precious metals, or an increase in the efficiency of the banking expedients by which these metals are economized;* in other words, in a saving and uninvesting period of the national industry, we accumulate gold and augment the efficiency of our gold: if therefore such a saving period follows close upon an occasion when foreign credits have been diminished and foreign debts called in, the augmentation in the effective quantity of gold in the country is extremely great. The old money called in from abroad and the new money representing the new saving co-operate with one another; and their natural tendency is, to cause a general rise in price, and what is the same thing, a diffused diminution in the purchasing power of money.

Up to this point there is nothing special in the recent history of the money market: similar events happened both after the panic of 1847 and after that of 1857. But there is another cause of the same kind, and acting in the same direction, which is peculiar to

the present time; this cause is the amount of the foreign money, and especially of the money of foreign governments, now in London. No government probably ever had nearly as much at its command as the German government now has. Speaking broadly, two things happened: during the war, England was the best place of shelter for foreign money, and this made money more cheap here than it would otherwise have been; after the war, England became the most convenient paying place and the most convenient resting place for money, and this again has made money cheaper. The commercial causes, for which there are many precedents, have been aided by a political cause for the efficacy of which there is no precedent.

But though plentiful money is necessary to high prices, and though it has a natural tendency to produce these prices, yet it is not of itself sufficient to produce them. In the cases we are dealing with, in order to lower prices, there must not only be additional money but a satisfactory mode of employing that additional money. This is obvious if we remember whence that augmented money is derived: it is derived from the savings of the people, and will only be invested in the manner which the holders for the time being consider suitable to such savings. It will not be used in mere expenditure,—it would be contrary to the very nature of it so to use it. A new channel of demand is required to take off the new money, or that new money will not raise prices: it will lie idle in the banks, as we have often seen it; we should still see the frequent, the common phenomenon of dull trade and cheap money existing side by side.

The demand in this case arose in the most effective of all ways. In 1867 and the first half of 1868 corn was dear, as the following figures show:—

'GAZETTE' AVERAGE PRICE OF WHEAT.

	s.	d.		s.	d.
December, 1866,	60	3	October, 1867,	66	6
January, 1867,	61	4	November, "	69	5
February, "	60	10	December, "	67	4
March, "	59	9	January, 1868,	70	3
April, "	61	6	February, "	73	0
May, "	64	8	March, "	73	0
June, "	65	4	April, "	73	3
July, "	65	0	May, "	73	9
August, "	67	8	June, "	67	11
September, "	62	8	July, "	65	5

From that time it fell, and it was very cheap during the whole of 1869 and 1870. The effect of this cheapness is great in every department of industry. The working classes, having cheaper food, need to spend so much less on that food, and have more to spend on other things: in consequence, there is a gentle augmentation of demand through almost all departments of trade; and this almost always causes a great augmentation in what may be called the "instrumental" trades, — that is, in the trades which deal in machines and instruments used in many branches of commerce, and in the materials for such. Take for instance the iron trade: —

			Tons.	Tons.
In the year	1869	we exported . .	2,568,000	
"	1870	" . .	2,716,000	
				5,284,000
"	1867	" . .	1,882,000	
"	1868	" . .	1,944,000	
				3,826,000
	Increase, ...			1,458,000

That is to say, cheap corn, operating throughout the world, created a new demand for many kinds of articles; the production of a large number of such articles being aided by iron in some one of its many forms, iron to that extent was exported. And the effect is cumulative: the manufacture of iron being stimulated, all persons concerned in that great manufacture are well off, have more to spend, and by spending it encourage other branches of manufacture, which again propagate the demand; they receive and so encourage industries in a third degree dependent and removed.

It is quite true that corn has not been quite so cheap during the present year; but even if it had been dearer than it is, it would not all at once arrest the great trade which former cheapness had created. The "ball," if we may so say, "was set rolling" in 1869 and 1870, and a great increase of demand was then created in certain trades and propagated through all trades. A continuance of very high prices would produce the reverse effect: it would slacken demand in certain trades, and the effect would be gradually diffused through all trades; but a slight rise such as that of this year has no perceptible effect.

When the stimulus of cheap corn is added to that of cheap money, the full conditions of a great and diffused rise of prices are satisfied. This new employment supplies a mode in which money can be invested. Bills are drawn of greater number and greater magnitude, and through the agencies of banks and discount

houses the savings of the country are invested in such bills; there is thus a new want, and a new purchase money to supply that want, and the consequence is the diffused and remarkable rise of price which the figures show to have occurred.

The rise has also been aided by the revival of credit; this, as need not be at length explained, is a great aid to buying, and consequently a great aid to a rise of price. Since 1866, credit has been gradually though very slowly recovering, and it is probably as good as it is reasonable or proper that it should be: we are now trusting as many people as we ought to trust, and as yet there is no wild excess of misplaced confidence which would make us trust those whom we ought not to trust.

The process thus explained is the common process. The surplus of loanable capital which lies in the hands of bankers is not employed by them in any original way; it is almost always lent to a trade already growing and already improving. The use of it develops that trade yet farther, and this again augments and stimulates other trades. Capital may long lie idle in a stagnant condition of industry: the mercantile securities which experienced bankers know to be good do not augment, and they will not invent other securities or take bad ones.

In most great periods of expanding industry, the three great causes — much loanable capital, good credit, and the increased profits derived from better used labor and better used capital — have acted simultaneously; and though either may act by itself, there is a permanent reason why mostly they will act together, — they both tend to grow together, if you begin from a period of depression. In such periods, credit is bad and industry unemployed; very generally provisions are high in price, and their dearness was one of the causes which made the times bad. Whether there was or was not too much loanable capital when that period begins, there soon comes to be too much. Quiet people continue to save part of their incomes in bad times as well as in good; indeed, of the two, people of slightly varying

and fixed incomes have better means of saving in bad times, because prices are lower. Quiescent trade affords no new securities in which the new saving can be invested, and therefore there comes soon to be an excess of loanable capital. In a year or two after a crisis, credit usually improves, as the remembrance of the disasters which at the crisis impaired credit is becoming fainter and fainter; provisions get back to their usual price, or some great industry makes, from some temporary cause, a quick step forward: at these moments, therefore, the three agencies which, as has been explained, greatly develop trade, combine to develop it simultaneously.

The certain result is a bound of national prosperity; the country leaps forward as if by magic: but only part of that prosperity has a solid reason. As far as prosperity is based on a greater quantity of production, and that of the right articles, as far as it is based on the increased rapidity with which commodities of every kind reach those who want them, its basis is good; human industry is more efficient, and therefore there is more to be divided among mankind: but in so far as that prosperity is based on a general rise of prices, it is only imaginary. A general rise of prices is a rise only in name: whatever any one gains on the article which he has to sell he loses on the articles which he has to buy, and so he is just where he was. The only real effects of a general rise of prices are these: — First, it straitens people of fixed incomes, who suffer as purchasers, but who have no gain to correspond. And secondly, it gives an extra profit to fixed capital created before the rise happened; here the sellers gain, but without any equivalent loss as buyers. Thirdly, this gain on fixed capital is greatest in what may be called the industrial "implements," such as coal and iron: these are wanted in all industries, and in any general increase of prices they are sure to rise much more than other things; everybody

wants them, the supply of them cannot be rapidly augmented, and therefore their price rises very quickly. But to the country as a whole, the general rise of prices is no benefit at all; it is simply a change of nomenclature for an identical relative value in the same commodities. Nevertheless, most people are happier for it, — they think they are getting richer, though they are not; and as the rise does not happen on all articles at the same moment, but is propagated gradually through society, those to whom it first comes gain really; and as at first every one believes that he will gain when his own article is rising, a buoyant cheerfulness overflows the mercantile world.

This prosperity is precarious as far as it is real, and transitory in so far as it is fictitious. The augmented production, which is the reason of the real prosperity, depends on the full working of the whole industrial organization, — of all capitalists and laborers; that prosperity was caused by that full working, and will cease with it: but that full working is liable to be destroyed by the occurrence of any great misfortune to any considerable industry, — this would cause misfortune to the industries dependent on that one, and, as has been explained, all through society and *back again*. But every such industry is liable to grave fluctuations, and the most important — the provision industries — to the gravest and the suddenest: they are dependent on the casualties of the seasons. A single bad harvest diffused over the world, a succession of two or three bad harvests even in England only, will raise the price of corn exceedingly and will keep it high; and a great and protracted rise in the price of corn will at once destroy all the real part of the unusual prosperity of previous good times. It will change the full working of the industrial machine into an imperfect working; it will make the produce of that machine less than usual instead of more than usual; instead of there

being more than the average of general dividend to be distributed between the producers, there will immediately be less than the average.

And in so far as the apparent prosperity is caused by an unusual plentifulness of loanable capital and a consequent rise in prices, that prosperity is not only liable to reaction but *certain* to be exposed to reaction: the same causes which generate this prosperity will, after they have been acting a little longer, generate an equivalent adversity. The process is this:— The plentifulness of loanable capital causes a rise of prices; that rise of prices makes it necessary to have more loanable capital to carry on the same trade. £100,000 will not buy as much when prices are high as it will when prices are low,—it will not be so effectual for carrying on business: more money is necessary in dear times than in cheap times to produce the same changes in the same commodities. Even supposing trade to have remained stationary, a greater capital would be required to carry it on after such a rise of prices as has been described than was necessary before that rise: but in this case the trade will *not* have remained stationary,—it will have increased, certainly to some extent, probably to a great extent; the "loanable capital," the lending of which caused the rise of prices, was lent to enable it to augment. The loanable capital lay idle in the banks till some trade started into prosperity, and then was lent in order to develop that trade; that trade caused other secondary developments; those secondary developments enabled more loanable capital to be lent, and that lending caused a tertiary development of trade: and so on through society.

In consequence, a long-continued low rate of interest is almost always followed by a rapid rise in that rate. Till the available trade is found it lies idle, and can scarcely be lent at all; some of it is not lent: but the moment the available trade is discovered,—the moment that prices have risen,—the

demand for loanable capital becomes keen. For the most part, men of business must carry on their regular trade; if it cannot be carried on without borrowing 10 per cent. more capital, 10 per cent. more capital they must borrow. Very often they have incurred obligations which must be met; and if that is so, the rate of interest which they pay is comparatively indifferent. What is necessary to meet their acceptances they will borrow, pay for it what they may; they had better pay any price than permit those acceptances to be dishonored. And in less extreme cases, men of business have a fixed capital which cannot lie idle except at a great loss; a set of laborers which must be if possible kept together; a steady connection of customers which they would very unwillingly lose: to keep all these, they borrow; and in a period of high prices many merchants are peculiarly anxious to borrow, because the augmentation of the price of the article in which they deal makes them really see, or imagine that they see, peculiar opportunities of profit. An immense new borrowing soon follows upon the new and great trade, and the rate of interest rises at once and generally rises rapidly.

This is the surer to happen that Lombard Street is, as has been shown before, a very delicate market. A large amount of money is held there by bankers and by bill-brokers at interest; this they must employ, or they will be ruined. It is better for them to reduce the rate they charge and compensate themselves by reducing the rate they pay, rather than to keep up the rate of charge if by so doing they cannot employ all their money; it is vital to them to employ all the money on which they pay interest: a little excess therefore forces down the rate of interest very much. But if that low rate of interest should cause or should aid in causing a great growth of trade, the rise is sure to be quick and is apt to be violent: the figures of trade are reckoned by hundreds of millions

where those of loanable capital count only by millions. A great increase in the borrowing demands of English commerce almost always changes an excess of loanable capital above the demand to a greater deficiency below the demand; that deficiency causes adversity or apparent adversity in trade, just as, and in the same manner that, the previous excess caused prosperity or apparent prosperity, — it causes a fall of price that runs through society; that fall causes a decline of activity and a diminution of profits, — a painful contraction instead of the previous pleasant expansion.

The change is generally quicker because some check to credit happens at an early stage of it. The mercantile community will have been unusually fortunate if during the period of rising prices it has not made great mistakes. Such a period naturally excites the sanguine and the ardent; they fancy that the prosperity they see will last always, that it is only the beginning of a greater prosperity. They altogether overestimate the demand for the article they deal in or the work they do; they all in their degree — and the ablest and the cleverest the most — work much more than they should, and trade far above their means. Every great crisis reveals the excessive speculations of many houses which no one before suspected, and which commonly indeed had not begun or had not carried very far those speculations till they were tempted by the daily rise of price and the surrounding fever.

The case is worse, because at most periods of great commercial excitement there is some mixture of the older and simpler kind of investing mania. Though the money of saving persons is in the hands of banks, and though, by offering interest, banks retain the command of much of it, yet they do not retain the command of the whole or anything near the whole: all of it can be used, and much of it is used, by its owners; they speculate with it in bubble companies

and in worthless shares, just as they did in the time of the South Sea mania when there were no banks, and as they would again in England supposing that banks ceased to exist. The mania of 1825 and the mania of 1866 were striking examples of this: in their case to a great extent, as in most similar modern periods to a less extent, the delirium of ancient gambling co-operated with the milder madness of modern overtrading. At the very beginning of adversity, the counters in the gambling mania, the shares in the companies created to feed the mania, are discovered to be worthless: down they all go, and with them much of credit.

The good times, too, of high price almost always engender much fraud. All people are most credulous when they are most happy; and when much money has just been made, when some people are really making it, when most people think they are making it, there is a happy opportunity for ingenious mendacity. Almost everything will be believed for a little while; and long before discovery, the worst and most adroit deceivers are geographically or legally beyond the reach of punishment. But the harm they have done diffuses harm, for it weakens credit still further.

When we understand that Lombard Street is subject to severe alternations of opposite causes, we should cease to be surprised at its seeming cycles; we should cease, too, to be surprised at the sudden panics: during the period of reaction and adversity, just even at the last instant of prosperity, the whole structure is delicate. The peculiar essence of our banking system is an unprecedented trust between man and man; and when that trust is much weakened by hidden causes, a small accident may greatly hurt it, and a great accident for a moment may almost destroy it.

Now too that we comprehend the inevitable vicissitudes of Lombard Street, we can also thoroughly

comprehend the cardinal importance of always retaining a great banking reserve: whether the times of adversity are well met or ill met depends far more on this than on any other single circumstance. If the reserve be large, its magnitude sustains credit; and if it be small, its diminution stimulates the gravest apprehensions. And the better we comprehend the importance of the banking reserve, the higher we shall estimate the responsibility of those who keep it.

CHAPTER VII.

A MORE EXACT ACCOUNT OF THE MODE IN WHICH THE BANK OF ENGLAND HAS DISCHARGED ITS DUTY OF RETAINING A GOOD BANK RESERVE, AND OF ADMINISTERING IT EFFECTUALLY.

THE preceding chapters have in some degree enabled us to appreciate the importance of the duties which the Bank of England is bound to discharge as to its banking reserve.

If we ask how the Bank of England has discharged this great responsibility, we shall be struck by three things: *first*, as has been said before, the Bank has never by any corporate act or authorized utterance acknowledged the duty, and some of its directors deny it; *second* (what is even more remarkable), no resolution of Parliament, no report of any committee of Parliament (as far as I know), no remembered speech of a responsible statesman, has assigned or enforced that duty on the Bank; *third* (what is more remarkable still), the distinct teaching of our highest authorities has often been that no public duty of any kind is imposed on the Banking Department of the Bank, — that for banking purposes it is only a joint-stock bank like any other bank, that its managers should look only to the interest of the proprietors and their dividend, that they are to manage as the London and Westminster Bank or the Union Bank manages.

At first it seems exceedingly strange that so important a responsibility should be unimposed, unacknowledged, and denied; but the explanation is this: we are living amid the vestiges of old controversies, and we speak their language, though we are

dealing with different thoughts and different facts. For more than fifty years — from 1793 down to 1844 — there was a keen controversy as to the public duties of the Bank. It was said to be the "manager" of the paper currency: and on that account many expected much good from it, others said it did great harm, others again that it could do neither good nor harm; but for the whole period there was an incessant and fierce discussion. That discussion was terminated by the Act of 1844: by that Act the currency manages itself; the entire working is automatic. The Bank of England plainly does not manage — cannot even be said to manage — the currency any more; and naturally, but rashly, the only reason upon which a public responsibility used to be assigned to the Bank having now clearly come to an end, it was inferred by many that the Bank had no responsibility.

The complete uncertainty as to the degree of responsibility acknowledged by the Bank of England is best illustrated by what has been said by the Bank directors themselves as to the panic of 1866. The panic of that year, it will be remembered, happened, contrary to precedent, in the spring; and at the next meeting of the court of Bank proprietors — the September meeting — there was a very remarkable discussion, which I give at length below,* and of which all that is most material was thus described in the *Economist*: —

THE GREAT IMPORTANCE OF THE LATE MEETING OF THE PROPRIETORS OF THE BANK OF ENGLAND.

THE late meeting of the proprietors of the Bank of England has a very unusual importance. There can be no effectual inquiry now into the history of the late crisis; a parliamentary committee next year would, unless something strange occur in the interval, be a great waste of time: men of business have keen sensations but short memories, and they will care no more next February for the events of last May than they now care for the events of October,

* See Note D in Appendix.

1864. A *pro forma* inquiry, on which no real mind is spent and which every one knows will lead to nothing, is far worse than no inquiry at all. Under these circumstances, the official statements of the Governor of the Bank are the only authentic expositions we shall have of the policy of the Bank directors, whether as respects the past or the future; and when we examine the proceedings with care, we shall find that they contain matter of the gravest import.

This meeting may be considered to admit and recognize the fact that the Bank of England keeps the sole banking reserve of the country. We do not now mix up this matter with the country circulation, or the question whether there should be many issuers of notes or only one; we speak not of the currency reserve, but of the banking reserve, — the reserve held against deposits, and not the reserve held against notes. We have often insisted in these columns that the Bank of England does keep the sole real reserve — the sole considerable unoccupied mass of cash — in the country; but there has been no universal agreement about it. Great authorities have been unwilling to admit it: they have not indeed formally and explicitly contended against it, — if they had, they must have pointed out some other great store of unused cash besides that at the Bank, and they could not find such store; but they have attempted distinctions, — have said that the doctrine that the Bank of England keeps the sole banking reserve of the country was "not a good way of putting it," was exaggerated, and was calculated to mislead.

But the late meeting is a complete admission that such is the fact. The Governor of the Bank said: —

"A great strain has within the last few months been put upon the resources of this house, and of the whole banking community of London; and I think I am entitled to say that not only this house, but the entire banking body, acquitted themselves most honorably and creditably throughout that very trying period. Banking is a very peculiar business, and it depends so much upon credit that the least blast of suspicion is sufficient to sweep away, as it were, the harvest of a whole year; but the manner in which the banking establishments generally of London met the demands made upon them during the greater portion of the past half-year affords a most satisfactory proof of the soundness of the principles on which their business is conducted. This house exerted itself to the utmost — and exerted itself most successfully — to meet the crisis; we did not flinch from our post. When the storm came upon us, on the morning on which it became known that the house of Overend & Co. had failed, we were in as sound and healthy a position as any banking establishment could hold, and on that day and throughout the succeeding

week we made advances which would hardly be credited; I do not believe that any one would have thought of predicting, even at the shortest period beforehand, the greatness of those advances. It was not unnatural that in this state of things a certain degree of alarm should have taken possession of the public mind, and that those who required accommodation from the Bank should have gone to the Chancellor of the Exchequer and requested the Government to empower us to issue notes beyond the statutory amount, if we should think that such a measure was desirable. But we had to act before we could receive any such power; and before the Chancellor of the Exchequer was perhaps out of his bed we had advanced one-half of our reserves, which were certainly thus reduced to an amount which we could not witness without regret. But we could not flinch from the duty which we conceived was imposed upon us of supporting the banking community, and I am not aware that any legitimate application for assistance made to this house was refused. Every gentleman who came here with adequate security was liberally dealt with; and if accommodation could not be afforded to the full extent which was demanded, no one who offered proper security failed to obtain relief from this house."*

Now, this is distinctly saying that the other banks of the country need not keep any such banking reserve — any such sum of actual cash, of real sovereigns and bank notes — as will help them through a sudden panic. It acknowledges a "duty" on the part of the Bank of England to "support the banking community," — to make the reserve of the Bank of England do for them as well as for itself.

In our judgment this language is most just, and the Governor of the Bank could scarcely have done a greater public service than by using language so business-like and so distinct. Let us know precisely who is to keep the banking reserve: if the joint-stock banks and the private banks and the country banks are to keep their share, let us determine on that, — Mr. Gladstone appeared not long since to say in Parliament that it ought to be so, — but at any rate there should be no doubt whose duty it is. Upon grounds which we have often stated, we believe that the anomaly of one bank keeping the sole banking reserve is so fixed in our system that we cannot change it if we would; the great evil to be feared was an indistinct conception of the fact, and that is now avoided.

* The text as given in this copy from the *Economist* differs trivially in the original from that given in the Appendix; I have followed the latter as most likely to be authentic. — Ed.

The importance of these declarations by the Bank is greater, because after the panic of 1857 the Bank did not hold exactly the same language. A person who loves concise expressions said lately that "Overends broke the Bank in 1866 because it went, and in 1857 because it was not let go." We need not too precisely examine such language; the element of truth in it is very plain, — the great advances made to Overends were a principal event in the panic of 1857. The bill-brokers were then very much what the bankers were lately, — they were the borrowers who wanted sudden and incalculable advances; but the bill-brokers were told not to expect the like again. But Alderman Salomons, on the part of the London bankers, said "he wished to take that opportunity of stating that he believed nothing could be more satisfactory to the managers and shareholders of joint-stock banks than the testimony which the Governor of the Bank of England had that day borne to the sound and honorable manner in which their business was conducted. It was manifestly desirable that the joint-stock banks and the banking interest generally should work in harmony with the Bank of England; and he sincerely thanked the Governor of the Bank for the kindly manner in which he had alluded to the mode in which the joint-stock banks had met the late monetary crisis." The Bank of England agrees to give other banks the requisite assistance in case of need, and the other banks agree to ask for it.

Secondly, the Bank agrees, in fact if not in name, to make unlimited advances on proper security to any one who applies for it. On the present occasion £45,000,000 was so advanced in three months: and the Bank do not say to the mercantile community, or to the bankers, "Do not come to us again: we helped you once, but do not look upon it as a precedent, — we will not help you again;" on the contrary, the evident and intended implication is, that under like circumstances the Bank would act again as it has now acted.

This article was much disliked by many of the Bank directors, and especially by some whose opinion is of great authority; they thought that the *Economist* drew "rash deductions" from a speech which was in itself "open to some objection," — which was, like all such speeches, defective in theoretical precision, and which was at best only the expression of an opinion by the Governor of that day, which had not been authorized by the Court of Directors, which

could not bind the Bank. However, the article had at least this use, that it brought out the facts. All the directors would have felt a difficulty in commenting upon, or limiting, or in differing from, a speech of a Governor from the chair; but there was no difficulty or delicacy in attacking the *Economist.* Accordingly Mr. Hankey, one of the most experienced Bank directors, not long after took occasion to observe:—

"The *Economist* newspaper has put forth what in my opinion is the most mischievous doctrine ever broached in the monetary or banking world in this country; viz., that it is the proper function of the Bank of England to keep money available at all times to supply the demands of bankers who have rendered their own assets unavailable. Until such a doctrine is repudiated by the banking interest, the difficulty of pursuing any sound principle of banking in London will be always very great. But I do not believe that such a doctrine as that bankers are justified in relying on the Bank of England to assist them in time of need is generally held by the bankers in London.

"I consider it to be the undoubted duty of the Bank of England to hold its banking deposits (reserving generally about one-third in cash) in the most available securities; and in the event of a sudden pressure in the money market, by whatever circumstance it may be caused, to bear its full share of a drain on its resources. I am ready to admit, however, that a general opinion has long prevailed that the Bank of England ought to be prepared to do much more than this, though I confess my surprise at finding an advocate for such an opinion in the *Economist.** If it were practicable for the Bank to retain money unemployed to meet such an emergency, it would be a very unwise thing to do so; but I contend that it is quite impracticable, and if it were possible, it would be most inexpedient: and I can only express my regret that the Bank, from a desire to do everything in its power to afford general assistance in times of banking or commercial distress, should ever have acted in a way to encourage such an opinion. The more the conduct of the affairs of the Bank is made to assimilate to the conduct of every other well-managed bank in the United Kingdom, the better for the Bank and the better for the community at large."

* *Vide Economist* of Sept. 22, 1866.

I am scarcely a judge, but I do not think Mr. Hankey replies to the *Economist* very conclusively.

First. He should have observed that the question is not as to what "ought to be," but as to what is. The *Economist* did not say that the system of a single bank reserve was a good system, but that it was the system which existed, and which must be worked, as you could not change it.

Secondly. Mr. Hankey should have shown "some other store of unused cash," except the reserve in the Banking Department of the Bank of England, out of which advances in time of panic could be made. These advances are necessary, and must be made by some one. The "reserves" of London bankers are not such store: they are *used* cash, not unused; they are part of the Bank deposits, and lent as such.

Thirdly. Mr. Hankey should have observed that we know by the published figures that the joint-stock banks of London do not keep one-third or anything like one-third of their liabilities in "cash," — even meaning by "cash" a deposit at the Bank of England: one-third of the deposits in joint-stock banks, not to speak of the private banks, would be £30,000,000, and the private deposits of the Bank of England are £18,000,000. According to his own statement there is a conspicuous contrast: the joint-stock banks — and the private banks, no doubt, too — keep one sort of reserve, and the Bank of England a different kind of reserve altogether. Mr. Hankey says that the two ought to be managed on the same principle; but if so, he should have said whether he would assimilate the practice of the Bank of England to that of the other banks, or that of the other banks to the practice of the Bank of England.

Fourthly. Mr. Hankey should have observed that, as has been explained, in most panics the principal use of a "banking reserve" is not to advance to bankers; the largest amount is almost always advanced to the mercantile public and to bill-brokers.

But the point is, that by our system all extra pressure is thrown upon the Bank of England. In the worst part of the crisis of 1866, £50,000 "fresh money" could not be borrowed, even on the best security, — even on consols, — except at the Bank of England; there was no other lender to new borrowers.

But my object now is not to revive a past controversy, but to show in what an unsatisfactory and uncertain condition that controversy has left a most important subject. Mr. Hankey's is the last explanation we have had of the policy of the Bank; he is a very experienced and attentive director, and I think expresses more or less the opinions of other directors: and what do we find? Setting aside and saying nothing about the remarkable speech of the Governor in 1866, which (at least according to the interpretation of the *Economist*) was clear and excellent, Mr. Hankey leaves us in doubt altogether as to what will be the policy of the Bank of England in the next panic, and as to what amount of aid the public may then expect from it. His words are too vague: no one can tell what a "fair share"* means, still less can we tell what other people at some future time will say it means. Theory suggests, and experience proves, that in a panic the holders of the ultimate bank reserve (whether one bank or many) should lend to all that bring good securities quickly, freely, and readily: by that policy they allay a panic, by every other policy they intensify it. The public have a right to know whether the Bank of England — the holders of our ultimate bank reserve — acknowledge this duty and are ready to perform it; but this is now very uncertain.

If we refer to history, and examine what in fact has been the conduct of the Bank directors, we find that they have acted exactly as persons of their type, character, and position might have been expected to act. They are a board of plain, sensible, prosperous English merchants; and they have both done and left

*Full share." See page 110.

undone what such a board might have been expected to do and not to do. Nobody could expect great attainments in economical science from such a board: laborious study is for the most part foreign to the habits of English merchants. Nor could we expect original views on banking; for banking is a special trade, and English merchants as a body have had no experience in it. A "board" can scarcely ever make improvements; for the policy of a board is determined by the opinions of the most numerous class of its members, — its average members, — and these are never prepared for sudden improvements. A board of upright and sensible merchants will always act according to what it considers "safe" principles, — that is, according to the *received* maxims of the mercantile world then and there; and in this manner the directors of the Bank of England have acted nearly uniformly.

Their strength and their weakness were curiously exemplified at the time when they had the most power. After the suspension of cash payments in 1797, the directors of the Bank of England could issue what notes they liked: there was no check; these notes could not come back upon the Bank for payment. There was a great temptation to extravagant issue, and no present penalty upon it: but the directors of the Bank withstood the temptation, — they did not issue their inconvertible notes extravagantly; and the proof is, that for more than ten years after the suspension of cash payments the Bank paper was undepreciated, and circulated at no discount in comparison with gold. Though the Bank directors of that day at last fell into errors, yet on the whole they acted with singular judgment and moderation. But when, in 1810, they came to be examined as to their reasons, they gave answers that have become almost classical by their nonsense. Mr. Pearse, the Deputy-Governor of the Bank, said: —

"In considering this subject, with reference to the manner in which bank notes are issued, resulting from the applications made

for discounts to supply the necessary want of bank notes, by which their issue in amount is so controlled that it can never amount to an excess, I cannot see how the amount of bank notes issued can operate upon the price of bullion or the state of the exchanges; and therefore I am individually of opinion that the price of bullion or the state of the exchanges can never be a reason for lessening the amount of bank notes to be issued, always understanding the control which I have already described."

"Is the Governor of the Bank of the same opinion which has now been expressed by the Deputy-Governor?"

Mr. WHITMORE — "I am so much of the same opinion, that I never think it necessary to advert to the price of gold or the state of the exchange on the days on which we make our advances."

"Do you advert to these two circumstances with a view to regulate the general amount of your advances?" — "I do not advert to it with a view to our general advances, conceiving it not to bear upon the question."

And Mr. Harman, another Bank director, expressed his opinion in these terms: — "I must very materially alter my opinions before I can suppose that the exchanges will be influenced by any modifications of our paper currency."

Very few persons perhaps could have managed to commit so many blunders in so few words.

But it is no disgrace at all to the Bank directors of that day to have committed these blunders: they spoke according to the best mercantile opinion of England. The City of London and the House of Commons both approved of what they said; those who dissented were said to be "abstract thinkers" and "unpractical men." The Bank directors adopted the ordinary opinions and pursued the usual practice of their time; it was this "routine" that caused their moderation. They believed that so long as they issued "notes" only at 5 per cent., and only on the discount of good bills, those notes could not be depreciated; and as the number of "good" bills — bills which sound merchants know to be good — does not rapidly increase, and as the market rate of interest was often less than 5 per cent., these checks on

over-issue were very effective. They failed in time, and the theory upon which they were defended was nonsense; but for a time their operation was powerful and excellent.

Unluckily, in the management of the matter before us, — the management of the bank reserve, — the directors of the Bank of England were neither acquainted with right principles nor were they protected by a judicious routine. They could not be expected themselves to discover such principles: the abstract thinking of the world is never to be expected from persons in high places; the administration of first-rate current transactions is a most engrossing business, and those charged with them are usually but little inclined to think on points of theory, even when such thinking most nearly concerns those transactions. No doubt when men's own fortunes are at stake, the instinct of the trader does somehow anticipate the conclusions of the closet; but a board has no instincts when it is not getting an income for its members, and when it is only discharging a duty of office. During the suspension of cash payments — a suspension which lasted twenty-two years — all traditions as to a cash reserve had died away; after 1819 the Bank directors had to discharge the duty of keeping a banking reserve, and (as the law then stood) a currency reserve also, without the guidance either of keen interests or good principles or wise traditions.

Under such circumstances, the Bank directors inevitably made mistakes of the gravest magnitude.

The first time of trial came in 1825. In that year the Bank directors allowed their stock of bullion to fall in the most alarming manner: —

	£.
On Dec. 24, 1824, the coin and bullion in the Bank was	10,721,000
On Dec. 25, 1825, it was reduced to . . .	1,260,000

and the consequence was a panic so tremendous that its results are well remembered after nearly fifty

years. In the next period of extreme trial — in 1837–9 — the Bank was compelled to draw for £2,000,000 on the Bank of France; and even after that aid the directors permitted their bullion, which was still the currency reserve as well as the banking reserve, to be reduced to £2,404,000: a great alarm pervaded society, and generated an eager controversy out of which ultimately emerged the Act of 1844. The next trial came in 1847, and then the Bank permitted its banking reserve (which the law had now distinctly separated) to fall to £1,176,000; and so intense was the alarm that the executive Government issued a letter of license, permitting the Bank if necessary to break the new law, and if necessary to borrow from the currency reserve, which was full, in aid of the banking reserve, which was empty. Till 1857 there was an unusual calm in the money market; but in the autumn of that year the Bank directors let the banking reserve, which even in October was far too small, fall thus: —

	£
Oct. 30,*	4,024,000
" 17,	3,217,000
" 24,	3,485,000
" 31,	2,258,000
Nov. 6,	2,155,000
" 13,	957,000

And then a letter of license like that of 1847 was not only issued but used: the ministry of the day authorized the Bank to borrow from the currency reserve in aid of the banking reserve, and the Bank of England did so borrow several hundred† pounds till the end of the month of November. A more miserable catalogue than that of the failures of the Bank of England to keep a good banking reserve, in all the seasons of trouble between 1825 and 1857, is scarcely to be found in history.

*"30" is a palpable error for "10." — Ed.

†"Thousand" is evidently omitted here. — Ed.

But since 1857 there has been a great improvement: by painful events and incessant discussions, men of business have now been trained to see that a large banking reserve is necessary, and to understand that in the curious constitution of the English banking world, the Bank of England is the only body which could effectually keep it. They have never acknowledged the duty; some of them, as we have seen, deny the duty: still, they have to a considerable extent begun to perform the duty. The Bank directors, being experienced and able men of business, comprehended this like other men of business; since 1857 they have always kept — I do not say a sufficient banking reserve, but — a fair and creditable banking reserve, and one altogether different from any which they kept before. At one period the Bank directors even went farther: they made a distinct step in advance of the public intelligence; they adopted a particular mode of raising the rate of interest, which is far more efficient than any other mode. Mr. Goschen observes, in his book on the Exchanges: —

"Between the rates in London and Paris, the expense of sending gold to and fro having been reduced to a minimum between the two cities, the difference can never be very great; but it must not be forgotten that — the interest being taken at a percentage calculated per annum, and the probable profit having, when an operation in three-month bills is contemplated, to be divided by four, whereas the percentage of expense has to be wholly borne by the one transaction, — a very slight expense becomes a great impediment. If the cost is only ½ per cent., there must be a profit of 2 per cent. in the rate of interest, or ½ per cent. on three months, before any advantage commences; and thus, supposing that Paris capitalists calculate that they may send their gold over to England for ½ per cent. expense, and chance their being so favored by the exchanges as to be able to draw it back without any cost at all, there must nevertheless be an excess of more than 2 per cent. in the London rate of interest over that in Paris before the operation of sending gold over from France, merely for the sake of the higher interest, will pay."

Accordingly, Mr. Goschen recommended that the Bank of England should, as a rule, raise their rate by steps

of 1 per cent. at a time when the object of the rise was to affect the "foreign exchanges"; and the Bank of England, from 1860 onward, have acted upon that principle. Before that time they used to raise their rate almost always by steps of ½ per cent., and there was nothing in the general state of mercantile opinion to compel them to change their policy; the change was, on the contrary, most unpopular. On this occasion, and as far as I know on this occasion alone, the Bank of England made an excellent alteration of their policy which was not exacted by contemporary opinion, and which was in advance of it.

The beneficial results of the improved policy of the Bank were palpable and speedy: we were enabled by it to sustain the great drain of silver from Europe to India to pay for Indian cotton in the years between 1862 and 1865. In the autumn of 1864 there was especial danger; but by a rapid and able use of their new policy, the Bank of England maintained an adequate reserve, and preserved the country from calamities which, if we had looked only to precedent, would have seemed inevitable. All the causes which produced the panic of 1857 were in action in 1864; the drain of silver in 1864 and the preceding year was beyond comparison greater than in 1857 and the years before it: and yet in 1864 there was no panic. The Bank of England was almost immediately rewarded for its adoption of right principles by finding that those principles, at a severe crisis, preserved public credit.

In 1866 undoubtedly a panic occurred; but I do not think that the Bank of England can be blamed for it. They had in their till an exceedingly good reserve according to the estimate of that time, — a sufficient reserve, in all probability, to have coped with the crises of 1847 and 1857: the suspension of Overend & Gurney — the most trusted private firm in England — caused an alarm in suddenness and magnitude without example. What was the effect of the

Act of 1844 on the panic of 1866, is a question on which opinion will be long divided; but I think it will be generally agreed that, acting under the provisions of that law, the directors of the Bank of England had in their Banking Department in that year a fairly large reserve — quite as large a reserve as any one expected them to keep — to meet unexpected and painful contingencies.

From 1866 to 1870 there was almost an unbroken calm on the money market. The Bank of England had no difficulties to cope with; there was no opportunity for much discretion; the money market took care of itself: but in 1870 the Bank of France suspended specie payments, and from that time a new era begins. The demands on this market for bullion have been greater and have been more incessant than they ever were before; for this is now the only bullion market. This has made it necessary for the Bank of England to hold a much larger banking reserve than was ever before required, and to be much more watchful than in former times lest that banking reserve should on a sudden be dangerously diminished; the forces are greater and quicker than they used to be, and a firmer protection and a surer solicitude are necessary: but I do not think the Bank of England is sufficiently aware of this, — all the governing body of the Bank certainly are not aware of it. The same eminent director to whom I have before referred, Mr. Hankey, published in the *Times* an elaborate letter, saying again that one-third of the liabilities were, even in these altered times, a sufficient reserve for the Banking Department of the Bank of England, and that it was no part of the business of the Bank to keep a supply of "bullion for exportation"; which was exactly the most mischievous doctrine that could be maintained when the Banking Department of the Bank of England had become the only great repository in Europe where gold could at once be obtained, and when

therefore a far greater store of bullion ought to be kept than at any former period.

And besides this defect of the present time, there are some chronic faults in the policy of the Bank of England, which arise, as will be presently explained, from grave defects in its form of government.

There is almost always some hesitation when a Governor begins to reign. He is the Prime Minister of the Bank Cabinet; and when so important a functionary changes, naturally much else changes too. If the Governor be weak, this kind of vacillation and hesitation continues throughout his term of office. The usual defect then is, that the Bank of England does not raise the rate of interest sufficiently quickly. It does raise it; in the end it takes the alarm: but it does not take the alarm sufficiently soon. A cautious man in a new office does not like strong measures. Bank Governors are generally cautious men, — they are taken from a most cautious class; in consequence they are very apt to temporize and delay: but almost always the delay in creating a stringency only makes a greater stringency inevitable. The effect of a timid policy has been to let the gold out of the Bank, and that gold *must* be recovered; it would really have been far easier to maintain the reserve by timely measures than to replenish it by delayed measures, — but new Governors rarely see this.

Secondly, those defects are apt, in part or as a whole, to be continued throughout the reign of a weak Governor. The objection to a decided policy, and the indisposition to a timely action, which are excusable in one whose influence is beginning and whose reign is new, are continued through the whole reign of one to whom those defects are natural, and who exhibits those defects in all his affairs.

Thirdly, this defect is enhanced because, as has so often been said, there is now no adequate rule recognized in the management of the banking reserve.

Mr. Weguelin, the last Bank Governor who has been examined, said that it was sufficient for the Bank to keep from one-fourth to one-third of its banking liabilities as a reserve; but no one now would ever be content if the banking reserve were near to one-fourth of its liabilities. Mr. Hankey, as I have shown, considers "about a third" as the proportion of reserve to liability at which the Bank should aim; but he does not say whether he regards a third as the minimum below which the reserve in the Banking Department should never be, or as a fair average about which the reserve may fluctuate, sometimes being greater or at others less.

In a future chapter I shall endeavor to show that one-third of its banking liabilities is at present by no means an adequate reserve for the Banking Department, — that it is not even a proper minimum, far less a fair average; and I shall allege what seem to me good reasons for thinking that unless the Bank aim by a different method at a higher standard, its own position may hereafter be perilous, and the public may be exposed to disaster.

II.

But as has been explained, the Bank of England is bound according to our system not only to keep a good reserve against a time of panic, but to use that reserve effectually when that time of panic comes. The keepers of the banking reserve, whether one or many, are obliged then to use that reserve for their own safety: if they permit all other forms of credit to perish, their own will perish immediately and in consequence.

As to the Bank of England, however, this is denied. It is alleged that the Bank of England can keep aloof in a panic; that it can, if it will, let other banks and trades fail; that if it chooses, it can stand alone, and survive intact while all else perishes

around it. On various occasions, most influential persons, both in the government of the Bank and out of it, have said that such was their opinion; and we must at once see whether this opinion is true or false, for it is absurd to attempt to estimate the conduct of the Bank of England during panics before we know what the precise position of the Bank in a panic really is.

The holders of this opinion in its most extreme form say that in a panic the Bank of England can stay its hand at any time; that though it has advanced much, it may refuse to advance more; that though the reserve may have been reduced by such advances, it may refuse to lessen it still further; that it can refuse to make any further discounts; that the bills which it has discounted will become due, that it can refill its reserve by the payment of those bills; that it can sell stock or other securities, and so replenish its reserve still further. But in this form the notion scarcely merits serious refutation: if the Bank reserve has once become low, there are in a panic no means of raising it again. Money parted with at such a time is very hard to get back; those who have taken it will not let it go, — not, at least, unless they are sure of getting other money in its place. And at such instant the recovery of money is as hard for the Bank of England as for any one else, probably even harder. The difficulty is this: if the Bank decline to discount, the holders of the bills previously discounted cannot pay. As has been shown, trade in England is largely carried on with borrowed money; if you propose greatly to reduce that amount, you will cause many failures unless you can pour in from elsewhere some equivalent amount of new money. But in a panic there is no new money to be had; everybody who has it clings to it, and will not part with it. Especially what has been advanced to merchants cannot easily be recovered: they are under immense liabilities, and they will

not give back a penny which they imagine that even possibly they may need to discharge those liabilities. And bankers are in even greater terror: in a panic they will not discount a host of new bills; they are engrossed with their own liabilities and those of their own customers, and do not care for those of others. The notion that the Bank of England can stop discounting in a panic, and so obtain fresh money, is a delusion. It can stop discounting, of course, at pleasure; but if it does it will get in no new money, — its bill case will daily be more and more packed with bills "returned unpaid."

The sale of stock, too, by the Bank of England in the middle of a panic is impossible: the Bank at such a time is the only lender on stock, and it is only by loans from a bank that large purchases at such a moment can be made; unless the Bank of England lend, no stock will be bought, — there is not in the country any large sum of unused ready money ready to buy it. The only unused sum is the reserve in the Banking Department of the Bank of England: if therefore in a panic that department itself attempt[ed] to sell stock, the failure would be ridiculous; it would hardly be able to sell any at all, — probably it would not sell £50 worth. The idea that the Bank can during a panic replenish its reserve in this or in any other manner, when that reserve has once been allowed to become empty or nearly empty, is too absurd to be steadily maintained, though I fear that it is not yet wholly abandoned.

The second and more reasonable conception of the independence of the Bank of England is, however, this: — It may be said, and it is said, that if the Bank of England stop at the beginning of a panic, if it refuse to advance a shilling more than usual, if it begin the battle with a good banking reserve and do not diminish it by extra loans, the Bank of England is sure to be safe. But this form of the opinion, though more reasonable and moderate, is not

therefore more true. The panic of 1866 is the best instance to test it. As every one knows, that panic began quite suddenly, on the fall of "Overends." Just before, the Bank had £5,812,000 in its reserve; in fact it advanced £13,000,000 of new money in the next few days, and its reserve went down to nothing, and the government had to help: but if the Bank had not made these advances, could it have kept its reserve?

Certainly it could not; it could not have retained its own deposits. A large part of these are the deposits of bankers, and they would not consent to help the Bank of England in a policy of isolation; they would not agree to suspend payments themselves, and permit the Bank of England to survive and get all their business. They would withdraw their deposits from the Bank; they would not assist it to stand erect amid their ruin. But even if this were not so, even if the banks were willing to keep their deposits at the Bank while it was not lending, they would soon find that they could not do it: they are only able to keep those deposits at the Bank by the aid of the Clearing House system; and if a panic were to pass a certain height, that system, which rests on confidence, would be destroyed by terror.

The common course of business is this:—A B, having to receive £50,000 from C D, takes C D's check on a banker "crossed," as it is called, and therefore only payable to another banker. He pays that check to his own credit with his own banker, who presents it to the banker on whom it is drawn, and if good it is an item between them in the general clearing or settlement of the afternoon. But this is evidently a very refined machinery, which a panic will be apt to destroy. At the first stage, A B may say to his debtor C D, "I cannot take your check, I must have bank notes;" if it is a debt on securities, he will be very apt to say this. The usual practice—credit being good—is for the creditor

to take the debtor's check and to give up the securities; but if the "securities" really secure him in a time of difficulty, he will not like to give them up and take a bit of paper,—a mere check, which may be paid or not paid: he will say to his debtor, "I can only give you your securities if you will give me bank notes;" and if he does say so, the debtor must go to his bank, and draw out the £50,000 if he has it. But if this were done on a large scale, the bank's "cash in house" would soon be gone; as the Clearing House was gradually superseded, it would have to trench on its deposit at the Bank of England; and then the bankers would have to pay so much over the counter that they would be unable to keep much money at the Bank, even if they wished,—they would soon be obliged to draw out every shilling.

The diminished use of the Clearing House in consequence of the panic would intensify that panic. By far the greater part of the bargains of the country in moneyed securities is settled on the Stock Exchange twice a month; and the number of securities then given up for mere checks, and the number of checks then passing at the Clearing House, are enormous: if that system collapse[d], the number of failures would be incalculable, and each failure would add to the discredit that caused the collapse.

The non-banking customers of the Bank of England would be discredited as well as other people; their checks would not be taken any more than those of others: they would have to draw out bank notes, and the Bank reserve would not be enough for a tithe of such payments.

The matter would come shortly to this:—A great number of brokers and dealers are under obligations to pay immense sums, and in common times they obtain these sums by the transfer of certain securities. If, as we said just now, No. 1 has borrowed £50,000 of No. 2 on Exchequer bills, he for the most part

cannot pay No. 2 till he has sold or pledged those bills to some one else: but till he has the bills he cannot pledge or sell them; and if No. 2 will not give them up till he gets his money, No. 1 will be ruined, because he cannot pay it. And if No. 2 has No. 3 to pay, as is very likely, he may be ruined because of No. 1's default, and No. 4 only on account of No. 3's default; and so on without end. On settling day, without the Clearing House, there would be a mass of failures and a bundle of securities. The effect of these failures would be a general run on all bankers, and on the Bank of England particularly.

It may indeed be said that the money thus taken from the Banking Department of the Bank of England would return there immediately; that the public who borrowed it would not know where else to deposit it; that it would be taken out in the morning and put back in the evening. But in the first place, this argument assumes that the Banking Department would have enough money to pay the demands on it; and this is a mistake, — the Banking Department would not have a hundredth part of the necessary funds. And in the second, a great panic which deranged the Clearing House would soon be diffused all through the country. The money, therefore, taken from the Bank of England could not be soon returned to the Bank; it would not come back on the evening of the day on which it was taken out, or for many days: it would be distributed through the length and breadth of the country, wherever there were bankers, wherever there was trade, wherever there were liabilities, wherever there was terror.

And even in London, so immense a panic would soon impair the credit of the Banking Department of the Bank of England. That department has no great *prestige:* it was only created in 1844, and it has failed three times since. The world would imagine that what has happened before will happen again; and when they have got money, they will

not deposit it at an establishment which may not be able to repay it. This did not happen in former panics, because the case we are considering never arose; the Bank was helping the public, and, more or less confidently, it was believed that the government would help the Bank: but if the policy be relinquished which formerly assuaged alarm, that alarm will be protracted and enhanced till it touches the Banking Department of the Bank itself.

I do not imagine that it would touch the Issue Department: I think that the public would be quite satisfied if they obtained bank notes. Generally, nothing is gained by holding the notes of a bank instead of depositing them at a bank; but in the Bank of England there is a great difference, — their notes are *legal tender*. Whoever holds them can always pay his debts; and except for foreign payments he could want no more. The rush would be for bank notes: those that could be obtained would be carried north, south, east, and west; and as there would not be enough for all the country, the Banking Department would soon pay away all it had.

Nothing, therefore, can be more certain than that the Bank of England has in this respect no peculiar privilege: that it is simply in the position of a bank keeping the banking reserve of the country; that it must in time of panic do what all other similar banks must do; that in time of panic it must advance freely and vigorously to the public out of the reserve.

And with the Bank of England, as with other banks in the same case, these advances, if they are to be made at all, should be made so as, if possible, to obtain the object for which they are made; the end is to stay the panic, and the advances should if possible stay the panic: and for this purpose there are two rules: —

First. That these loans should only be made at a very high rate of interest; this will operate as a

heavy fine on unreasonable timidity, and will prevent the greatest number of applications by persons who do not require it. The rate should be raised early in the panic, so that the fine may be paid early; that no one may borrow out of idle precaution without paying well for it; that the banking reserve may be protected as far as possible.

Secondly. That at this rate these advances should be made on all good banking securities, and as largely as the public ask for them. The reason is plain: the object is to stay alarm, and nothing therefore should be done to cause alarm; but the way to cause alarm is to refuse some one who has good security to offer. The news of this will spread in an instant through all the money market at a moment of terror; no one can say exactly who carries it, but in half an hour it will be carried on all sides, and will intensify the terror everywhere. No advances indeed need be made by which the Bank will ultimately lose. The amount of bad business in commercial countries is an infinitesimally small fraction of the whole business; that in a panic the bank or banks holding the ultimate reserve should refuse bad bills or bad securities will not make the panic really worse, — the "unsound" people are a feeble minority, and they are afraid even to look frightened for fear their unsoundness may be detected. The great majority, the majority to be protected, are the "sound" people, the people who have good security to offer. If it is known that the Bank of England is freely advancing on what in ordinary times is reckoned a good security, — on what is then commonly pledged and easily convertible, — the alarm of the solvent merchants and bankers will be stayed; but if securities really good and usually convertible are refused by the Bank, the alarm will not abate, the other loans made will fail in obtaining their end, and the panic will become worse and worse.

It may be said that the reserve in the Banking

Department will not be enough for all such loans. If that be so, the Banking Department must fail; but lending is nevertheless its best expedient, — this is the method of making its money go the farthest, and of enabling it to get through the panic if anything will so enable it. Making no loans, as we have seen, will ruin it; making large loans and stopping, as we have also seen, will ruin it. The only safe plan for the Bank is the brave plan, — to lend in a panic on every kind of current security, or every sort on which money is ordinarily and usually lent. This policy may not save the Bank; but if it do not, nothing will save it.

If we examine the manner in which the Bank of England has fulfilled these duties, we shall find, as we found before, that the true principle has never been grasped; that the policy has been inconsistent; that though the policy has much improved, there still remain important particulars in which it might be better than it is.

The first panic of which it is necessary here to speak is that of 1825. I hardly think we should derive much instruction from those of 1793 and 1797, — the world has changed too much since; and during the long period of inconvertible currency from 1797 to 1819, the problems to be solved were altogether different from our present ones. In the panic of 1825, the Bank of England at first acted as unwisely as it was possible to act: by every means it tried to restrict its advances; the reserve being very small, it endeavored to protect that reserve by lending as little as possible. The result was a period of frantic and almost inconceivable violence: scarcely any one knew whom to trust; credit was almost suspended; the country was, as Mr. Huskisson expressed it, "within twenty-four hours of a state of barter." Applications for assistance were made to the Government; but though it was well known that the Government refused to act, there was not, as far as I know, until

lately any authentic narrative of the real facts. In the Correspondence of the Duke of Wellington, of all places in the world, there is a full account of them. The Duke was then on a mission at St. Petersburg, and Sir R. Peel wrote to him a letter of which the following is a part:—

"We have been placed in a very unpleasant predicament on the other question, — the issue of Exchequer bills by Government. The feeling of the City, of many of our friends, of some of the Opposition, was decidedly in favor of the issue of Exchequer bills to relieve the merchants and manufacturers.

"It was said in favor of the issue, that the same measure had been tried and succeeded in 1793 and 1811. Our friends whispered about that we were acting quite in a different manner from that in which Mr. Pitt did act, and would have acted had he been alive.

"We felt satisfied that however plausible were the reasons urged in favor of the issue of Exchequer bills, yet that the measure was a dangerous one, and ought to be resisted by the Government.

"There are thirty millions of Exchequer bills outstanding; the purchases lately made by the Bank can hardly maintain them at par. If there were a new issue to such an amount as that contemplated, — viz., five millions, — there would be a great danger that the whole mass of Exchequer bills would be at a discount, and would be paid into the revenue. If the new Exchequer bills were to be issued at a different rate of interest from the outstanding ones, — say bearing an interest of five per cent., — the old ones would be immediately at a great discount unless the interest were raised; if the interest were raised, the charge on the revenue would be of course proportionate to the increase of rate of interest. We found that the Bank had the power to lend money on deposit of goods: as our issue of Exchequer bills would have been useless unless the Bank cashed them, as therefore the intervention of the Bank was in any event absolutely necessary, and as its intervention would be chiefly useful by the effect which it would have in increasing the circulating medium, we advised the Bank to take the whole affair into their own hands at once, — to issue their notes on the security of goods instead of issuing them on Exchequer bills, such bills being themselves issued on that security.

"They reluctantly consented, and rescued us from a very embarrassing predicament."

The success of the Bank of England on this occasion was owing to its complete adoption of right principles. The Bank adopted these principles very late; but when it adopted them it adopted them completely. According to the official statement which I quoted before, "We" (that is, the Bank directors) lent money "by every possible means, and in modes which we had never adopted before: we took in stock on security, we purchased Exchequer bills, we made advances on Exchequer bills; we not only discounted outright, but we made advances on the deposit of bills of exchange to an immense amount, — in short, by every possible means consistent with the safety of the Bank." And for the complete and courageous adoption of this policy at the last moment, the directors of the Bank of England at that time deserve great praise, for the subject was then less understood even than it is now: but the directors of the Bank deserve also severe censure, for previously choosing a contrary policy; for being reluctant to adopt the new one, and for at last adopting it only at the request of, and upon a joint responsibility with, the executive Government.

After 1825 there was not again a real panic in the money market till 1847. Both of the crises of 1837 and 1839 were severe, but neither terminated in a panic; both were arrested before the alarm reached its final intensity: in neither, therefore, could the policy of the Bank at the last stage of fear be tested.

In the three panics since 1844 — in 1847, 1857, and 1866 — the policy of the Bank has been more or less affected by the Act of 1844, and I cannot therefore discuss it fully within the limits which I have prescribed for myself. I can only state two things: — First, that the directors of the Bank above all things maintain that they have not been in the earlier stage of panic prevented by the Act of 1844 from making any advances which they would otherwise have then

made. Secondly, that in the last stage of panic, the Act of 1844 has been already suspended, rightly or wrongly, on these occasions; that no similar occasion has ever yet occurred in which it has not been suspended; and that, rightly or wrongly, the world confidently expects and relies that in all similar cases it will be suspended again. Whatever theory may prescribe, the logic of facts seems peremptory so far; and these principles taken together amount to saying that by the doctrine of the directors, the Bank of England ought, as far as they can, to manage a panic with the Act of 1844 pretty much as they would manage one without it, — in the early stage of the panic because then they are not fettered, and in the latter because then the fetter has been removed.

We can therefore estimate the policy of the Bank of England in the three panics which have happened since the Act of 1844, without inquiring into the effect of the act itself. It is certain that in all of these panics the Bank has made very large advances indeed. It is certain, too, that in all of them the Bank has been quicker than it was in 1825; that in all of them it has less hesitated to use its banking reserve in making the advances which it is one principal object of maintaining that reserve to make, and to make at once. But there is still a considerable evil: no one knows on what kind of securities the Bank of England will at such periods make the advances which it is necessary to make.

As we have seen, principle requires that such advances, if made at all for the purpose of curing panic, should be made in the manner most likely to cure that panic; and for this purpose, they should be made on everything which in common times is good "banking security." The evil is, that owing to terror, what is commonly good security has ceased to be so: and the true policy is, so to use the banking reserve that if possible the temporary evil may be stayed and the common course of business be restored;

and this can only be effected by advancing on all good banking securities.

Unfortunately, the Bank of England do not take this course. The Discount office is open for the discount of good bills, and makes immense advances accordingly; the Bank also advances on consols and India securities, though there was in the crisis of 1866 believed to be for a moment a hesitation in so doing: but these are only a small part of the securities on which money in ordinary times can be readily obtained, and by which its repayment is fully secured. Railway debenture stock is as good a security as a commercial bill, and many people (of whom I own I am one) think it safer than India stock, — on the whole a great railway is, we think, less liable to unforeseen accidents than the strange Empire of India; but I doubt if the Bank of England in a panic would advance on railway debenture stock, — at any rate, no one has any authorized reason for saying that it would. And there are many other such securities.

The *amount* of the advance is the main consideration for the Bank of England, and not the nature of the security on which the advance is made, always assuming the security to be good. An idea prevails (as I believe) at the Bank of England, that they ought not to advance during a panic on any kind of security on which they do not commonly advance; but if bankers for the most part do advance on such security in common times, and if that security is indisputably good, the ordinary practice of the Bank of England is immaterial. In ordinary times the Bank is only one of many lenders, whereas in a panic it is the sole lender; and we want, as far as we can, to bring back the unusual state of a time of panic to the common state of ordinary times.

In common opinion there is always great uncertainty as to the conduct of the Bank: the Bank has never laid down any clear and sound policy on the

subject; as we have seen, some of its directors (like Mr. Hankey) advocate an erroneous policy. The public is never sure what policy will be adopted at the most important moment; it is not sure what amount of advance will be made, or on what security it will be made. The best palliative to a panic is a confidence in the adequate amount of the Bank reserve, and in the efficient use of that reserve; and until we have on this point a clear understanding with the Bank of England, both our liability to crises and our terror at crises will always be greater than they would otherwise be.

CHAPTER VIII.

THE GOVERNMENT OF THE BANK OF ENGLAND.

The Bank of England is governed by a Board of Directors, a Governor, and a Deputy-Governor; and the mode in which these are chosen, and the time for which they hold office, affect the whole of its business. The Board of Directors is in fact self-electing. In theory a certain portion go out annually, remain out for a year, and are subject to re-election by the proprietors: but in fact they are nearly always, and always if the other directors wish it, re-elected after a year; such has been the unbroken practice of many years, and it would be hardly possible now to break it. When a vacancy occurs by death or resignation, the whole board chooses the new member; and they do it, as I am told, with great care. For a peculiar reason, it is important that the directors should be young when they begin; and accordingly the board run over the names of the most attentive and promising young men in the old-established firms of London, and select the one who, they think, will be most suitable for a bank director. There is a considerable ambition to fill the office: the status which is given by it, both to the individual who fills it and to the firm of merchants to which he belongs, is considerable. There is surprisingly little favor shown in the selection; there is a great wish on the part of the Bank directors for the time being to provide, to the best of their ability, for the future good government of the Bank. Very few selections in the world are made with nearly equal purity. There is a

sincere desire to do the best for the Bank, and to appoint a well-conducted young man who has begun to attend to business, and who seems likely to be fairly sensible and fairly efficient twenty years later.

The age is a primary matter. The offices of Governor and Deputy-Governor are given in rotation; the Deputy-Governor always succeeds the Governor, and usually the oldest director who has not been in office becomes Deputy-Governor. Sometimes, from personal reasons, such as ill-health or special temporary occupation, the time at which a director becomes Deputy-Governor may be a little deferred; and in some few cases, merchants in the greatest business have been permitted to decline entirely: but for all general purposes the rule may be taken as absolute,—save in rare cases, a director must serve his time as Governor and Deputy-Governor nearly when his turn comes, and he will not be asked to serve much before his turn. It is usually about twenty years from the time of a man's first election that he arrives, as it is called, at the chair; and as the offices of Governor and Deputy-Governor are very important, a man who fills them should be still in the vigor of life: accordingly, Bank directors, when first chosen by the board, are always young men.

At first this has rather a singular effect; a stranger hardly knows what to make of it. Many years since, I remember seeing a very fresh and nice-looking young gentleman, and being struck with astonishment at being told that he was a director of the Bank of England. I had always imagined such directors to be men of tried sagacity and long experience, and I was amazed that a cheerful young man should be one of them; I believe I thought it was a little dangerous: I thought such young men could not manage the Bank well; I feared they had the power to do mischief.

Further inquiry, however, soon convinced me that they had not the power. Naturally, young men have

not much influence at a board where there are many older members; and in the Bank of England there is a special provision for depriving them of it if they get it. Some of the directors, as I have said, retire annually: but by courtesy it is always the young ones; those who have passed the chair — that is, who have served the office of Governor — always remain. The young part of the board is the fluctuating part, and the old part is the permanent part; and therefore it is not surprising that the young part has little influence. The Bank directors may be blamed for many things, but they cannot be blamed for the changeableness and excitability of a neocracy.

Indeed, still better to prevent it, the elder members of the board — that is, those who have passed the chair — form a standing committee of indefinite powers, which is called the Committee of Treasury. I say "indefinite powers"; for I am not aware that any precise description has ever been given of them, and I doubt if they can be precisely described. They are sometimes said to exercise a particular control over the relations and negotiations between the Bank and the Government; but I confess that I believe that this varies very much with the character of the Governor for the time being, — a strong Governor does much mainly upon his own responsibility, and a weak Governor does little. Still, the influence of the Committee of Treasury is always considerable, though not always the same. They form a cabinet of mature, declining, and old men, just close to the executive; and for good or evil, such a cabinet must have much power.

By old usage, the directors of the Bank of England cannot be themselves by trade bankers. This is a relic of old times: every bank was supposed to be necessarily more or less in opposition to every other bank, — banks in the same place to be especially in opposition; in consequence, in London, no banker has a chance of being a Bank director, or would ever

think of attempting to be one. I am here speaking of bankers in the English sense, and in the sense that would surprise a foreigner. One of the Rothschilds is on the Bank direction, and a foreigner would be apt to think that they were bankers if any one was; but this only illustrates the essential difference between our English notions of banking and the Continental, — ours have attained a much fuller development than theirs. Messrs. Rothschild are immense capitalists, having doubtless much borrowed money in their hands; but they do not take £100 payable on demand and pay it back in checks of £5 each, and that is our English banking. The borrowed money which they have is in large sums, borrowed for terms more or less long: English bankers deal with an aggregate of small sums, all of which are repayable on short notice or on demand. And the way the two employ their money is different also. A foreigner thinks "an exchange business" — that is, the buying and selling bills on foreign countries — a main part of banking; as I have explained, remittance is one of the subsidiary conveniences which early banks subserve before deposit banking begins: but the mass of English country bankers only give bills on places in England or on London, and in London the principal remittance business has escaped out of the hands of the bankers. Most of them would not know how to carry through a great "exchange operation," or to "bring home the returns"; they would as soon think of turning silk merchants. The exchange trade is carried on by a small and special body of foreign bill-brokers, of whom Messrs. Rothschild are the greatest. One of that firm may therefore well be on the Bank direction, notwithstanding the rule forbidding bankers to be there; for he and his family are not English bankers, either by the terms on which they borrow money or the mode in which they employ it. But as to bankers in the English sense of the word, the rule is rigid and

absolute: not only no private banker is a director of the Bank of England, but no director of any joint-stock bank would be allowed to become such; the two situations would be taken to be incompatible.

The mass of the Bank directors are merchants of experience, employing a considerable capital in trades in which they have been brought up and with which they are well acquainted. Many of them have information as to the present course of trade, and as to the character and wealth of merchants, which is most valuable — or rather is all but invaluable — to the Bank. Many of them, too, are quiet, serious men, who, by habit and nature, watch with some kind of care every kind of business in which they are engaged, and give an anxious opinion on it. Most of them have a good deal of leisure; for the life of a man of business who employs only his own capital, and employs it nearly always in the same way, is by no means fully employed. Hardly any capital is enough to employ the principal partner's time, and if such a man is very busy it is a sign of something wrong: either he is working at detail, which subordinates would do better and which he had better leave alone, or he is engaged in too many speculations, is incurring more liabilities than his capital will bear, and so may be ruined. In consequence, every commercial city abounds in men who have great business ability and experience, who are not fully occupied, who wish to be occupied, and who are very glad to become directors of public companies in order to be occupied. The direction of the Bank of England has for many generations been composed of such men.

Such a government for a joint-stock company is very good if its essential nature be attended to, and very bad if that nature be not attended to. That government is composed of men with a high average of general good sense, with an excellent knowledge of business in general, but without any special knowledge of the particular business in which they are

engaged. Ordinarily, in joint-stock banks and companies this deficiency is cured by the selection of a manager of the company, who has been specially trained to that particular trade, and who engages to devote all his experience and all his ability to the affairs of the company; the directors, and often a select committee of them more especially, consult with the manager, and after hearing what he has to say, decide on the affairs of the company. There is in all ordinary joint-stock companies a fixed executive specially skilled, and a somewhat varying council not specially skilled; the fixed manager insures continuity and experience in the management, and a good board of directors insures general wisdom.

But in the Bank of England there is no fixed executive: the Governor and Deputy-Governor, who form that executive, change every two years. I believe, indeed, that such was not the original intention of the founders: in the old days of few and great privileged companies, the chairman, though periodically elected, was practically permanent so long as his policy was popular; he was the head of the ministry, and ordinarily did not change unless the Opposition came in. But this idea has no present relation to the constitution of the Bank of England: at present the Governor and Deputy-Governor almost always change at the end of two years; the case of any longer occupation of the chair is so very rare that it need not be taken account of. And the Governor and Deputy-Governor of the Bank cannot well be shadows: they are expected to be constantly present; to see all applicants for advances out of the ordinary routine; to carry on the almost continuous correspondence between the Bank and its largest customer the Government; to bring all necessary matters before the Board of Directors or the Committee of Treasury, — in a word, to do very much of what falls to the lot of the manager in most companies. Under this shifting chief executive there are indeed

very valuable heads of departments; the head of the Discount Department is especially required to be a man of ability and experience. But these officers are essentially subordinate; no one of them is like the general manager of an ordinary bank, the head of all action: the perpetually present executive, the Governor and Deputy-Governor, make it impossible that any subordinate should have that position. A really able and active-minded Governor, being required to sit all day in the Bank, in fact does and can hardly help doing its principal business.

In theory, nothing can be worse than this government for a bank: a shifting executive; a board of directors chosen too young for it to be known whether they are able; a committee of management in which seniority is the necessary qualification and old age the common result; and no trained bankers anywhere.

Even if the Bank of England were an ordinary bank, such a constitution would be insufficient; but its inadequacy is greater, and the consequences of that inadequacy far worse, because of its greater functions. The Bank of England has to keep the sole banking reserve of the country; has to keep it through all changes of the money market and all turns of the exchanges; has to decide on the instant in a panic what sort of advances should be made, to what amounts, and for what dates: and yet it has a constitution plainly defective. So far from the government of the Bank of England being better than that of any other bank, — as it ought to be, considering that its functions are much harder and graver, — any one would be laughed at who proposed it as a model for the government of a new bank; and that government, if it were so proposed, would on all hands be called "old-fashioned" and "curious."

As was natural, the effects — good and evil — of its constitution are to be seen in every part of the

Bank's history. On one vital point, the Bank's management has been excellent: it has done perhaps less "bad business"—certainly less very bad business—than any bank of the same size and the same age. In all its history I do not know that its name has ever been connected with a single large and discreditable bad debt; there has never been a suspicion that it was "worked" for the benefit of any one man or any combination of men: the great respectability of the directors, and the steady attention many of them have always given the business of the Bank, have kept it entirely free from anything dishonorable and discreditable. Steady merchants collected in council are an admirable judge of bills and securities: they always know the questionable standing of dangerous persons; they are quick to note the smallest signs of corrupt transactions, and no sophistry will persuade the best of them out of their good instincts. You could not have made the directors of the Bank of England do the sort of business which "Overends" at last did, except by a moral miracle—except by changing their nature; and the fatal career of the Bank of the United States would, under their management, have been equally impossible. Of the ultimate solvency of the Bank of England, or of the eventual safety of its vast capital, even at the worst periods of its history, there has not been the least doubt.

But nevertheless, as we have seen, the policy of the Bank has frequently been deplorable; and at such times the defects of its government have aggravated if not caused its calamities.

In truth, the executive of the Bank of England is now much such as the executive of a public department—of the Foreign Office or the Home Office—would be in which there was no responsible permanent head. In these departments of Government, the actual chief changes nearly though not quite as often as the Governor of the Bank of England; the parliamentary Under-Secretary—the Deputy-Governor, so

to speak, of that office — changes nearly as often : and if the administration solely or in its details depended on these two, it would stop. New men could not carry it on with vigor and efficiency ; indeed, they could not carry it on at all : but in fact they are assisted by a permanent under-secretary, who manages all the routine business, who is the depository of the secrets of the office, who embodies its traditions, who is the *hyphen* between changing administrations. In consequence of this assistance, the continuous business of the department is for the most part managed sufficiently well, notwithstanding frequent changes in the heads of administration ; and it is only by such assistance that such business could be so managed. The present administration of the Bank is an attempt to manage a great, a growing, and a permanently continuous business without an adequate permanent element and a competent connecting link.

In answer, it may be said that the duties which press on the Governor and Deputy-Governor of the Bank are not so great or so urgent as those which press upon the heads of official departments. And perhaps in point of mere labor the Governor of the Bank has the advantage, — banking never ought to be an exceedingly laborious trade ; there must be a great want of system and a great deficiency in skilled assistance if extreme labor is thrown upon the chief : but in importance, the functions of the head of the Bank rank as high as those of any department, — the cash reserve of the country is as precious a deposit as any set of men can have the care of. And the difficulty of dealing with a panic (as the administration of the Bank is forced to deal with it) is perhaps a more formidable instant difficulty than presses upon any single minister ; at any rate it comes more suddenly, and must be dealt with more immediately, than most comparable difficulties : and the judgment, the nerve, and the vigor needful to deal with it are plainly rare and great.

The natural remedy would be, to appoint a permanent Governor of the Bank. Nor, as I have said, can there be much doubt that such was the intention of its founders. All the old companies which have their beginning in the seventeenth century had the same constitution, and those of them which have lingered down to our time retain it: the Hudson's Bay Company, the South Sea Company, the East India Company, were all founded with a sort of sovereign executive, intended to be permanent and intended to be efficient. This is indeed the most natural mode of forming a company in the minds of those to whom companies are new. Such persons will have always seen business transacted a good deal despotically; they will have learnt the value of prompt decision and of consistent policy; they will have often seen that business is best managed when those who are conducting it could scarcely justify the course they are pursuing by distinct argument which others could understand. All City people make their money by investments, for which there are often good argumentative reasons; but they would hardly ever be able, if required before a parliamentary committee, to state those reasons. They have become used to act on them without distinctly analyzing them, and — in a monarchical way — with continued success only as a test of their goodness. Naturally such persons, when proceeding to form a company, make it upon the model of that which they have been used to see successful: they provide for the executive first and above all things. How much this was in the minds of the founders of the Bank of England may be judged of by the name which they gave it: its corporate name is "The *Governor* and Company of the Bank of England"; so important did the founders think the executive that they mentioned it distinctly, and mentioned it first.

And not only is this constitution of a company the most natural in the early days when companies

were new, it is also that which experience has shown to be the most efficient now that companies have long been tried. Great railway companies are managed upon no other: scarcely any instance of great success in a railway can be mentioned in which the chairman has not been an active and judicious man of business, constantly attending to the affairs of the company; a thousand instances of railway disaster can be easily found in which the chairman was only a nominal head, — a nobleman, or something of that sort, chosen for show; "railway chairmanship" has become a profession, so much is efficiency valued in it and so indispensable has ability been found to be. The plan of appointing a permanent "chairman" at the Bank of England is strongly supported by much modern experience.

Nevertheless, I hesitate as to its expediency; at any rate, there are other plans which for several reasons should, I think, first be tried in preference.

First. This plan would be exceedingly unpopular. A permanent Governor of the Bank of England would be one of the greatest men in England. He would be a little "monarch" in the City; he would be far greater than the Lord Mayor. He would be the personal embodiment of the Bank of England; he would be constantly clothed with an almost indefinite *prestige.* Everybody in business would bow down before him and try to stand well with him, for he might in a panic be able to save almost any one he liked and to ruin almost any one he liked; a day might come when his favor might mean prosperity and his distrust might mean ruin. A position with so much real power and so much apparent dignity would be intensely coveted. Practical men would be apt to say that it was better than the Prime-Ministership; for it would last much longer, and would have a greater jurisdiction over that which practical men would most value, — over *money.* At all events, such a Governor, if he understood his business, might

make the fortunes of fifty men where the Prime Minister can make that of one. Scarcely anything could be more unpopular in the City than the appointment of a little king to reign over them.

Secondly. I do not believe that we should always get the best man for the post; often I fear that we should not even get a tolerable man. There are many cases in which the offer of too high a pay would prevent our obtaining the man we wish for, and this is one of them. A very high pay of *prestige* is almost always very dangerous: it causes the post to be desired by vain men, by lazy men, by men of rank; and when that post is one of real and technical business, and when therefore it requires much previous training, much continuous labor, and much patient and quick judgment, all such men are dangerous, — but they are sure to covet all posts of splendid dignity, and can only be kept out of them with the greatest difficulty. Probably in every Cabinet there are still some members (in the days of the old close boroughs there were many) whose posts have come to them not from personal ability or inherent merit, but from their rank, their wealth, or even their imposing exterior. The highest political offices are indeed kept clear of such people, for in them serious and important duties must constantly be performed in the face of the world: a Prime Minister or a Chancellor of the Exchequer or a Secretary of State must explain his policy and defend his actions in Parliament; and the discriminating tact of a critical assembly, abounding in experience and guided by tradition, will soon discover what he is. But the Governor of the Bank would only perform quiet functions, which look like routine though they are not, in which there is no immediate risk of success or* failure; which years hence may indeed issue in a crop of bad debts, but which any grave person may make at the time to look fair and plausible. A

*These last two words are nonsense, but I dare not disturb them. — Ed.

large bank is exactly the place where a vain and shallow person in authority, if he be a man of gravity and method, as such men often are, may do infinite evil in no long time and before he is detected; if he is lucky enough to begin at a time of expansion in trade, he is nearly sure not to be found out till the time of contraction has arrived, and then very large figures will be required to reckon the evil he has done.

And *thirdly.* I fear that the possession of such patronage would ruin any set of persons in whose gift it was. The election of the chairman must be placed either in the court of proprietors or that of the directors. If the proprietors choose, there will be something like the evils of an American presidential election. Bank stock will be bought in order to confer the qualification of voting at the election of the "chief of the City." The chairman, when elected, may well find that his most active supporters are large borrowers of the Bank, and he may well be puzzled to decide between his duty to the Bank and his gratitude to those who chose him. Probably if he be a cautious man of average ability, he will combine both evils: he will not lend so much money as he is asked for, and so will offend his own supporters; but will lend some which will be lost, and so the profits of the Bank will be reduced. A large body of bank proprietors would make but a bad elective body for an office of great *prestige:* they would not commonly choose a good person, and the person they did choose would be bound by promises that would make him less good.

The court of directors would choose better, — a small body of men of business would not easily be persuaded to choose an extremely unfit man; but they would not often choose an extremely good man. The really best man would probably not be so rich as the majority of the directors, nor of so much standing; and not unnaturally they would much dislike to

elevate to the headship of the City one who was much less in the estimation of the City than themselves. And they would be canvassed in every way and on every side to appoint a man of mercantile dignity or mercantile influence: many people of the greatest *prestige* and rank in the City would covet so great a dignity, if not for themselves at least for some friend or some relative, and so the directors would be set upon from every side.

An election so liable to be disturbed by powerful vitiating causes would rarely end in a good choice. The best candidate would almost never be chosen; often, I fear, one would be chosen altogether unfit for a post so important. And the excitement of so keen an election would altogether disturb the quiet of the Bank. The good and efficient working of a board of bank directors depends on its internal harmony; and that harmony would be broken forever by the excitement, the sayings, and the acts of a great election. The Board of Directors would almost certainly be demoralized by having to choose a sovereign; and there is no certainty, nor any great likelihood indeed, that they would choose a good one.

In France the difficulty of finding a good body to choose the Governor of the Bank has been met characteristically: the Bank of France keeps the money of the state, and the state appoints its Governor. The French have generally a logical reason to give for all they do, though perhaps the results of their actions are not always so good as the reasons for them: the Governor of the Bank of France has not always, I am told, been a very competent person; the Sub-Governor, whom the state also appoints, is, as we might expect, usually better. But for our English purposes it would be useless to inquire minutely into this: no English statesman would consent to be responsible for the choice of the Governor of the Bank of England. After every panic, the Opposition would say in Parliament that the calamity

had been "grievously aggravated," if not wholly caused, by the "gross misconduct" of the Governor appointed by the ministry. Or possibly offices may have changed occupants, and the ministry in power at the panic would be the opponents of the ministry which at a former time appointed the Governor: in that case they would be apt to feel, and to intimate, a "grave regret" at the course which the nominee of their adversaries had "thought it desirable to pursue"; they would not much mind hurting his feelings, and if he resigned they would have themselves a valuable piece of patronage to confer on one of their own friends. No result could be worse than that the conduct of the Bank and the* management should be made a matter of party politics; and men of all parties would agree in this, even if they agreed in almost nothing else.

I am therefore afraid that we must abandon the plan of improving the government of the Bank of England by the appointment of a permanent Governor; because we should not be sure of choosing a good Governor, and should indeed run a great risk for the most part of choosing a bad one.

I think, however, that much of the advantage, with little of the risk, might be secured by a humbler scheme. In English political offices, as was observed before, the evil of a changing head is made possible by the permanence of a dignified subordinate. Though the parliamentary Secretary of State and the parliamentary Under-Secretary go in and out with each administration, another under-secretary remains through all such changes, and is on that account called "permanent": now, this system seems to me in its principle perfectly applicable to the administration of the Bank of England. For the reasons which have just been given, a permanent ruler of the Bank of England cannot be appointed; for other reasons, which were just before given, *some* most

* Plainly a typographical error for "its." — Ed.

influential permanent functionary is essential in the proper conduct of the business of the Bank: and *mutatis mutandis*, these are the very difficulties and the very advantages which have led us to frame our principal offices of state in the present fashion.

Such a Deputy-Governor would not be at all a "king" in the City: there would be no mischievous *prestige* about the office, there would be no attraction in it for a vain man, and there would be nothing to make it an object of a violent canvass or of unscrupulous electioneering; the office would be essentially subordinate in its character, just like the permanent secretary in a political office. The pay should be high, for good ability is wanted; but no pay would attract the most dangerous class of people. The very influential but not very wise City dignitary who would be so very dangerous is usually very opulent, — he would hardly have such influence if he were not opulent: what he wants is not money, but "position." A Governorship of the Bank of England he would take almost without salary; perhaps he would even pay to get it: but a minor office of essential subordination would not attract him at all. We may augment the pay enough to get a good man, without fearing that by such pay we may tempt — as by social privilege we should tempt — exactly the sort of man we do not want.

Undoubtedly such a permanent official should be a trained banker. There is a cardinal difference between banking and other kinds of commerce: you can afford to run much less risk in banking than in commerce, and you must take much greater precautions. In common business, the trader can add to the cost price of the goods he sells a large mercantile profit, say 10 to 15 per cent.; but the banker has to be content with the interest of money, which in England is not so much as 5 per cent. upon the average: the business of a banker therefore cannot bear so many bad debts as that of a merchant,

and he must be much more cautious to whom he gives credit. Real money is a commodity much more coveted than common goods: for one deceit which is attempted on a manufacturer or a merchant, twenty and more are attempted on a banker. And besides, a banker, dealing with the money of others, and money payable on demand, must be always, as it were, looking behind him and seeing that he has reserve enough in store if payment should be asked for, which a merchant dealing mostly with his own capital need not think of. Adventure is the life of commerce, but caution (I had almost said timidity) is the life of banking; and I cannot imagine that the long series of great errors made by the Bank of England in the management of its reserve till after 1857, would have been possible if the merchants in the Bank court had not erroneously taken the same view of the Bank's business that they must properly take of their own mercantile business. The Bank directors have almost always been too cheerful as to the Bank's business, and too little disposed to take alarm. What we want to introduce into the Bank court is a wise *apprehensiveness;* and this every trained banker is taught by the habits of his trade and the atmosphere of his life.

The permanent Governor ought to give his whole time to the business of the Bank; he ought to be forbidden to engage in any other concern. All the present directors, including the Governor and Deputy-Governor, are engaged in their own business; and it is very possible — indeed, it must perpetually have happened — that their own business as merchants most occupied the minds of most of them just when it was most important that the business of the Bank should occupy them. It is at a panic and just before a panic that the business of the Bank is most exacting and most engrossing; but just at that time the business of most merchants must be unusually occupying, and may be exceedingly critical. By the

present constitution of the Bank, the attention of its sole rulers is most apt to be diverted from the Bank's affairs just when those affairs require that attention the most; and the only remedy is the appointment of a permanent and influential man, who will have no business save that of the Bank, and who therefore presumably will attend most to it at the critical instant when attention is most required. His mind at any rate will in a panic be free from pecuniary anxiety; whereas many if not all of the present directors must be incessantly thinking of their own affairs, and unable to banish them from their minds.

The permanent Deputy-Governor must be a director and a man of fair position; he must not have to say "Sir" to the Governor. There is no fair argument between an inferior who has to exhibit respect and a superior who has to receive respect. The superior can always, and does mostly, refute the bad arguments of his inferior, but the inferior rarely ventures to try to refute the bad arguments of his superior: and he still more rarely states his case effectually; he pauses, hesitates, does not use the best word or the most apt illustration, perhaps he uses a faulty illustration or a wrong word, and so fails because the superior immediately exposes him. Important business can only be sufficiently discussed by persons who can say very much what they like very much as they like to one another; the thought of the speaker should come out as it was in his mind, and not be hidden in respectful expressions or enfeebled by affected doubt. What is wanted at the Bank is not a new clerk to the directors, — they have excellent clerks of great experience now, — but a permanent equal to the directors, who shall be able to discuss on equal terms with them the business of the Bank, and have this advantage over them in discussion, that he has no other business than that of the Bank to think of.

The formal duties of such a permanent officer could only be defined by some one conversant with the business of the Bank, and could scarcely be intelligibly discussed before the public; nor are the precise duties of the least importance. Such an officer, if sound, able, and industrious, would soon rule the affairs of the Bank: he would be acquainted better than any one else both with the traditions of the past and with the facts of the present; he would have a great experience; he would have seen many anxious times, he would always be on the watch for their recurrence. And he would have a peculiar power of guidance at such moments from the nature of the men with whom he has most to deal. Most Governors of the Bank of England are cautious merchants, not profoundly skilled in banking, but most anxious that their period of office should be prosperous and that they should themselves escape censure; if a "safe" course is pressed upon them, they are likely to take that course. Now, it would almost always be "safe" to follow the advice of the great standing "authority"; it would always be most "unsafe" not to follow it. If the changing Governor act[ed] on the advice of the permanent Deputy-Governor, most of the blame in case of mischance would fall on the latter: it would be said that a shifting officer like the Governor might very likely not know what should be done, but that the permanent official was put there to know it and paid to know it. But if, on the other hand, the changing Governor should disregard the advice of his permanent colleague, and the consequence should be bad, he would be blamed exceedingly: it would be said that, "being without experience, he had taken upon him to overrule men who had much experience; that when the constitution of the Bank had provided them with skilled counsel, he had taken on himself to act of his own head and to disregard that counsel;" and so on *ad infinitum*. And there could be no sort

of conversation more injurious to a man in the City: the world there would say, rightly or wrongly, "We must never be too severe on errors of judgment,—we are all making them every day; if reasonable persons do their best, we can expect no more. But this case is different: the Governor acted on a wrong system, he took upon himself an unnecessary responsibility;" and so a Governor who incurred disaster by disregarding his skilled counselor would be thought a fool in the City forever. In consequence, the one-skilled counselor would in fact rule the Bank.

I believe that the appointment of the new permanent and skilled authority at the Bank is the greatest reform which can be made there, and that which is most wanted. I believe that such a person would give to the decision of the Bank that foresight, that quickness, and that consistency in which those decisions are undeniably now deficient. As far as I can judge, this change in the constitution of the Bank is by far the most necessary, and is perhaps more important even than all other changes; but nevertheless we should reform the other points which we have seen to be defective.

First, the London bankers should not be altogether excluded from the court of directors. The old idea, as I have explained, was, that the London bankers were the competitors of the Bank of England, and would hurt it if they could; but now the London bankers have another relation to the Bank, which did not then exist and was not then imagined. Among private people they are the principal depositors in the Bank: they are therefore particularly interested in its stability; they are especially interested in the maintenance of a good banking reserve, for their own credit and the safety of their large deposits depend on it. And they can bring to the court of directors an experience of banking itself, got outside the Bank of England, which none of the present directors possess, for *they* have learned all they know

of banking at the Bank itself. There was also an old notion that the secrets of the Bank would be divulged if they were imparted to bankers; but probably bankers are better trained to silence and secrecy than most people, and there is only a thin partition now between the bankers and the secrets of the Bank. Only lately a firm failed of which one partner was a director of the London and Westminster Bank, and another a director of the Bank of England: who can define or class the confidential communications of such persons under such circumstances?

As I observed before, the line drawn at present against bankers is very technical and exclusively English. According to Continental ideas, Messrs. Rothschild are bankers if any one is a banker: but the house of Rothschild is represented on the Bank direction; and it is most desirable that it should be represented, for members of that firm can give, if they choose, confidential information of great value to the Bank. But nevertheless, the objection which is urged against English bankers is at least equally applicable to these foreign bankers: they have or may have at certain periods an interest opposite to the policy of the Bank, — as the greatest exchange dealers, they may wish to export gold just when the Bank of England is raising its rate of interest to prevent any one from exporting gold. The vote of a great exchange dealer might be objected to for plausible reasons of contrary interest, if any such reasons were worth regarding; but in fact, the particular interest of single directors is not to be regarded. Almost all directors who bring special information labor under a suspicion of interest, — they can only have acquired that information in present business, and such business may very possibly be affected for good or evil by the policy of the Bank: but you must not on this account seal up the Bank hermetically against living information; you must make a

fair body of directors upon the whole, and trust that the bias of some individual interests will disappear and be lost in the whole. And if this is to be the guiding principle, it is not consistent to exclude English bankers from the court.

Objection is often also taken to the constitution of the Committee of Treasury. That body is composed of the Governor and Deputy-Governor and all the directors who have held those offices: but as those offices in the main pass in rotation, this mode of election very much comes to an election by seniority; and there are obvious objections to giving not only a preponderance to age, but a monopoly to age. In some cases, indeed, this monopoly I believe has already been infringed,—when directors have, on account of the magnitude of their transactions and the consequent engrossing nature of their business, declined to fill the chair, in some cases they have been asked to be members of the Committee of Treasury notwithstanding; and it would certainly upon principle seem wiser to choose a committee which for some purposes approximates to a committee of management by competence rather than by seniority.

An objection is also taken to the large number of Bank directors: there are twenty-four directors, a Governor, and a Deputy-Governor; making a total court of twenty-six persons, which is obviously too large for the real discussion of any difficult business. And the case is worse because the court only meets once a week, and only sits a very short time: it has been said, with exaggeration but not without a basis of truth, that if the Bank directors were to sit for four hours, there would be "a panic solely from that." "The court," says Mr. Tooke, "meets at half past eleven or twelve; and if the sitting be prolonged beyond half past one, the Stock Exchange and the money market become excited, under the idea that a change of importance is under discussion; and persons congregate about the doors of the Bank parlor

to obtain the earliest intimation of the decision." And he proceeds to conjecture that the knowledge of the impatience without must cause haste, if not impatience, within. That the decisions of such a court should be of incalculable importance is plainly very strange.

There should be no delicacy as to altering the constitution of the Bank of England. The existing constitution was framed in times that have passed away, and was intended to be used for purposes very different from the present. The founders may have considered that it would lend money to the government, that it would keep the money of the government, that it would issue notes payable to bearer; but that it would keep the "banking reserve" of a great nation, no one in the seventeenth century imagined. And when the use to which we are putting an old thing is a new use, in common-sense we should think whether the old thing is quite fit for the use to which we are setting it: "putting new wine into old bottles" is safe only when you watch the condition of the bottle, and adapt its structure most carefully.

CHAPTER IX.

THE JOINT-STOCK BANKS.

THE joint-stock banks of this country are a most remarkable success. Generally speaking, the career of joint-stock companies in this country has been checkered. Adam Smith, many years since, threw out many pregnant hints on the difficulty of such undertakings, — hints which even after so many years will well repay perusal; but joint-stock banking has been an exception to this rule.* Four years ago I threw together the facts on the subject and the reasons for them; and I venture to quote the article, because subsequent experience suggests, I think, little to be added to it.

"THE main classes of joint-stock companies which have answered are three: — *First.* Those in which the capital is used not to work the business but to *guarantee* the business. Thus, a banker's business — his proper business — does not begin while he is using his own money: it commences when he begins to use the capital of others. An insurance office in the long run needs no capital: the premiums which are received ought to exceed the claims which accrue. In both cases the capital is wanted to assure the public and to induce it to trust the concern. *Secondly.* Those companies have answered which have an exclusive privilege which they have used with judgment, or which possibly was so very profitable as to enable them to thrive with little judgment. *Thirdly.* Those which have undertaken a business both large and simple, — employing more money than most individuals or private firms have at command, and yet such that, in Adam Smith's words, 'the operations are capable of being reduced to a routine, or such a uniformity of method as admits of no variation.'

"As a rule, the most profitable of these companies are banks. Indeed, *all* the favoring conditions just mentioned concur in many

*Which Adam Smith (Book v., Chap. i.) distinctly says it is likely to be.— ED.

banks. An old-established bank has a '*prestige*' which amounts to a 'privileged opportunity': though no exclusive right is given to it by law, a peculiar power is given to it by opinion. The business of banking ought to be simple: if it is *hard* it is *wrong*. The only securities which a banker, using money that he may be asked at short notice to repay, ought to touch, are those which are easily salable and easily intelligible: if there is a difficulty or a doubt, the security should be declined. No business can of course be quite reduced to fixed rules; there must be occasional cases which no preconceived theory can define: but banking comes as near to fixed rules certainly as any existing business, perhaps as any possible business. The business of an old-established bank has the full advantage of being a simple business, and in part the advantage of being a monopoly business. Competition with it is only open in the sense in which competition with 'the London Tavern' is open: any one that has to do with either will pay dear for it.

"But the main source of the profitableness of established banking is the smallness of the requisite capital. Being only wanted as a 'moral influence,' it need not be more than is necessary to secure that influence. Although, therefore, a banker deals only with the most sure securities, and with those which yield the least interest, he can nevertheless gain and divide a very large profit upon his own capital, because the money in his hands is so much larger than that capital.

"Experience, as shown by plain figures, confirms these conclusions. We print at the end of this article the respective profits of 110 banks in England and Scotland and Ireland, being all in those countries of which we have sufficient information, — the Bank of England excepted. There are no doubt others, but they are not quoted even on local Stock Exchange lists, and in most cases publish no reports. The result of these banks, as regards the dividends they pay, is: —

	No. of Companies.	Capital.
		£
Above 20 per cent.,	15	5,302,767
Between 15 and 20 per cent.,	20	5,439,439
Between 10 and 15 per cent.,	36	14,056,950
Between 5 and 10 per cent.,	36	14,182,379
Under 5 per cent.,	3	1,350,000
	110	40,331,535

"That is to say, above 25 per cent. of the capital employed in these banks pays over 15 per cent., and 62½ per cent. of the capital pays more than 10 per cent. So striking a result is not to be shown in any other joint-stock trade.

"The period to which these accounts refer was certainly not a particularly profitable one; on the contrary, it has been specially unprofitable, — the rate of interest has been very low, and the amount of good security in the market small. Many banks — to some extent most banks — probably had in their books painful reminiscences of 1866;* the fever of excitement which passed over the nation was strongest in the classes to whom banks lent most, and consequently the losses of even the most careful banks (save of those in rural and sheltered situations) were probably greater than usual. But even tried by this very unfavorable test, banking is a trade profitable far beyond the average of trades.

"There is no attempt in these banks, on the whole and as a rule, to divide too much; on the contrary, they have accumulated about £13,000,000, or nearly one-third of their capital, principally out of undivided profits. The directors of some of them have been anxious to put away as much as possible and to divide as little as possible.

"The reason is plain: out of the banks which pay more than 20 per cent., all but one were old-established banks; and all those paying between 15 and 20 per cent. were old banks too. The 'privileged opportunity' of which we spoke is singularly conspicuous in such figures: it enables banks to pay much, which without it would *not* have paid much. The amount of the profit is clearly proportional to the value of the 'privileged opportunity': all the banks which pay above 20 per cent., save one, are banks more than 25 years old; all those which pay between 15 and 20 are so too. A new bank could not make these profits, or even by its competition much reduce these profits: in attempting to do so, it would simply ruin itself; not possessing the accumulated credit of years, it would have to wind up before it attained that credit.

"The value of the opportunity, too, is proportioned† to what has to be paid for it. Some old banks have to pay interest for all their money; some have much for which they pay nothing. Those who give much to their customers have of course less left for their shareholders. Thus Scotland, where there is always a daily interest, has no bank in the lists paying over 15 per cent. The profits of Scotch banks run thus: —

* The panic started by the failure of Overend, Gurney & Co — Ed.

† *Inversely* proportioned, as he goes on to show: evidently, the more it costs the less it is worth. — Ed.

	Capital. £	Dividend.
Bank of Scotland, ...	1,500,000	12
British Linen Company, . . .	1,000,000	13
Caledonian, ...	125,000	10
Clydesdale, ...	900,000	10
Commercial Bank of Scotland, .	1,000,000	13
National Bank of Scotland, . .	1,000,000	12
North of Scotland, ...	280,000	10
Union Bank of Scotland, . .	1,000,000	10
City of Glasgow, ...	870,000	8
Royal Bank, ...	2,000,000	8
	9,675,000	

"Good profits enough, but not at all like the profits of the London and Westminster, or the other most lucrative banks of the South.

"The Bank of England, it is true, does not seem to pay so much as other English banks in this way of reckoning; it makes an immense profit, but then its capital is immense too. In fact, the Bank of England suffers under two difficulties. Being much older than the other joint-stock banks, it belongs to a less profitable era: when it was founded, banks looked rather to the profit on their own capital and to the gains of note issue than to the use of deposits. The first relations with the state were more like those of a finance company than of a bank, as we now think of banking: if the Bank had not made loans to the government which we should now think dubious, the Bank would not have existed, for the government would never have permitted it. Not only is the capital of the Bank of England relatively greater, but the means of making profit in the Bank of England are relatively less also: by custom and understanding, the Bank of England keep a much greater reserve in unprofitable cash than other banks; if they do not keep it, either our whole system must be changed or we should break up in utter bankruptcy. The earning faculty of the Bank of England is in proportion less than that of other banks, and also the sum on which it has to pay dividend is altogether greater than theirs.

"It is interesting to compare the facts of joint-stock banking with the fears of it which were felt. In 1832 Lord Overstone observed: —

"I think that joint-stock banks are deficient in everything requisite for the conduct of the banking business except extended responsibility. The banking business requires peculiarly persons attentive

to all its details, — constantly, daily, and hourly watchful of every transaction, — much more than mercanti'e or trading business ; it also requires immediate prompt decisions upon circumstances when they arise, in many cases a decision that does not admit of delay for consultation ; it also requires a discretion to be exercised with reference to the special circumstances of each case. Joint-stock banks, being of course obliged to act through agents and not by a principal, and therefore under the restraint of general rules, cannot be guided by so nice a reference to degrees of difference in the character of responsibility of parties ; nor can they undertake to regulate the assistance to be granted to concerns under temporary embarrassment by so accurate a reference to the circumstances, favorable or unfavorable, of each case."

"But in this very respect, joint-stock banks have probably improved the business of banking. The old private banks in former times used to lend much to private individuals ; the banker, as Lord Overstone on another occasion explained, could have no security, but he formed his judgment of the discretion, the sense, and the solvency of those to whom he lent. And when London was by comparison a small city, and when by comparison every one stuck to his proper business, this practice might have been safe : but now that London is enormous and that no one can watch any one, such a trade would be disastrous ; at present it would hardly be safe in a country town. The joint-stock banks were quite unfit for the business Lord Overstone meant, but then that business is quite unfit for the present time."

This success of joint-stock banking is very contrary to the general expectation at its origin. Not only private bankers, such as Lord Overstone then was, but a great number of thinking persons, feared that the joint-stock banks would fast ruin themselves, and then cause a collapse and panic in the country ; the whole of English commercial literature between 1830 and 1840 is filled with that idea, nor did it cease in 1840. So late as 1845, Sir R. Peel thought the foundation of joint-stock banks so dangerous that he subjected it to grave and exceptional difficulty : under the Act of 1845 which he proposed, no such companies could be founded except with shares of £100, with £50 paid up on each ; which effectually checked the progress of such banks, for few new ones were

established for many years, or till that act had been repealed. But in this as in many other cases, perhaps Sir R. Peel will be found to have been clear-sighted rather than far-sighted. He was afraid of certain joint-stock banks which he saw rising around him; but the effect of his legislation was to give to these very banks, if not a monopoly, at any rate an exemption from new rivals. No one now founds or can found a new private bank, and Sir R. Peel by law prevented new joint-stock banks from being established; though he was exceedingly distrustful of the joint-stock banks founded between 1826 and 1845, yet in fact he was their especial patron, and he more than any other man encouraged and protected them.

But in this wonderful success there are two dubious points, two considerations of different kinds, which forbid us to say that in other countries, even in countries with the capacity of co-operation, joint-stock banks would succeed as well as we have seen that they succeed in England.

First, these great banks have not had to keep so large a reserve against their liabilities as it was natural that they should, being of first-rate magnitude, keep. They were at first, of course, very small in comparison with what they are now; they found a number of private bankers grouped round the Bank of England, and they added themselves to the group; not only did they keep their reserve from the beginning at the Bank of England, but they did not keep so much reserve as they would have kept if there had been no Bank of England. For a long time this was hardly noticed: for many years questions of the "currency," particularly questions as to the Act of 1844, engrossed the attention of all who were occupied with these subjects; even those who were most anxious to speak evil of joint-stock banks did not mention this particular evil. The first time, as far as I know, that it was commented on

in any important document, was in an official letter written in 1857 by Mr. Weguelin, who was then Governor of the Bank, to Sir George Lewis, who was then Chancellor of the Exchequer. The Governor and the directors of the Bank of England had been asked by Sir George Lewis severally to give their opinions on the Act of 1844, and all their replies were published; in his, Mr. Weguelin says:—

"If the amount of the reserve kept by the Bank of England be contrasted with the reserve kept by the joint-stock banks, a new and hitherto little considered source of danger to the credit of the country will present itself. The joint-stock banks of London, judging by their published accounts, have deposits to the amount of £30,000,000; their capital is not more than £3,000,000, and they have on an average £31,000,000 invested in one way or another: leaving only £2,000,000 as a reserve against all this mass of liabilities."

But these remarkable words were little observed in the discussions of that time,—the air was obscured by other matters; but in this work I have said so much on the subject that I need say little now. The joint-stock banks now keep a main part of their reserve on deposit with the bill-brokers, or in good and convertible interest-bearing securities; from these they obtain a large income, and that income swells their profits: if they had to keep a much larger part than now of that reserve in barren cash, their dividends would be reduced, and their present success would become less conspicuous.

The second misgiving, which many calm observers more and more feel as to our largest joint-stock banks, fastens itself on their government: is that government sufficient to lend well and keep safe so many millions? They are governed, as every one knows, by a board of directors, assisted by a general manager; and there are in London unrivaled materials for composing good boards of directors. There are very many men of good means, of great sagacity and great experience in business, who are obliged to

be in the City every day and to remain there during the day, but who have very much time on their hands. A merchant employing solely or principally his own capital has often a great deal of leisure. He is obliged to be on the market and to hear what is doing; every day he has some business to transact: but his transactions can be but few. His capital can bear only a limited number of purchases: if he bought as much as would fill his time from day to day he would soon be ruined, for he could not pay for it. Accordingly, many excellent men of business are quite ready to become members of boards of directors, and to attend to the business of companies, a good deal for the employment's sake; to have an interesting occupation which brings dignity and power with it pleases them very much. As the aggregation of commerce in great cities grows, the number of such men augments: a *council* of grave, careful, and experienced men can without difficulty be collected for a great bank in London, such as never could have been collected before, and such as cannot now be collected elsewhere.

There are facilities, too, for engaging a good banker to be a manager such as there never were before in the world. The number of such persons is much on the increase. Any careful person who is experienced in figures, and has real sound sense, may easily make himself a good banker: the modes in which money can be safely lent by a banker are not many, and a clear-headed, quiet, industrious person may soon learn all that is necessary about them. Our intricate law of real property is an impediment in country banking, for it requires some special study even to comprehend the elements of a law which is full of technical words, and which can only be explained by narrating its history; but the banking of great cities is little concerned with loans on landed property, and all the rest of the knowledge requisite for a banker can easily be obtained by any one who has

the sort of mind which takes to it. No doubt there is a vast *routine* of work to be learned, and the manager of a large bank must have a great facility in transacting business rapidly: but a great number of persons are now bred from their earliest manhood in the very midst of that routine; they learn it as they would learn a language, and come to be no more able to unlearn it than they could unlearn a language; and the able ones among them acquire an almost magical rapidity in effecting the business connected with that routine. A very good manager and very good board of directors can, without unreasonable difficulty, be provided for a bank at present in London.

It will be asked, What more can be required? I reply, A great deal. All which the best board of directors can really accomplish is, to form a good decision on the points which the manager presents to them, and perhaps on a few others which one or two zealous members of their body may select for discussion. A meeting of fifteen or eighteen persons is wholly unequal to the transaction of more business than this; it will be fortunate, and it must be well guided, if it should be found to be equal to so much. The discussion even of simple practical points by such a number of persons is a somewhat tedious affair: many of them will wish to speak on every decision of moment, and some of them — some of the best of them, perhaps — will only speak with difficulty and slowly. Very generally, several points will be started at once unless the discussion is strictly watched by a rigid chairman; and even on a single point the arguments will often raise grave questions which cannot be answered, and suggest many more issues than can be advantageously decided by the meeting. The time required by many persons for discussing many questions would alone prevent an assembly of many persons from overlooking a large and complicated business.

Nor is this the only difficulty: not only would a real supervision of a large business by a board of directors require much more time than the board would consent to occupy in meeting, it would also require much more time and much more thought than the individual directors would consent to give. These directors are only employing on the business of the bank the vacant moments of their time and the spare energies of their minds; they cannot give the bank more, — the rest is required for the safe conduct of their own affairs, and if they diverted it from these affairs they would be ruined. A few of them may have little other business, or they may have other partners in the business on whose industry they can rely and whose judgment they can trust; one or two may have retired from business: but for the most part, directors of a company cannot attend principally and anxiously to the affairs of a company without so far neglecting their own business as to run great risk of ruin; and if they are ruined, their trustworthiness ceases, and they are no longer permitted by custom to be directors.

Nor, even if it were possible really to supervise a business by the effectual and constant inspection of fifteen or sixteen rich and capable persons, would even the largest business easily bear the expense of such a supervision. I say "rich," because the members of a board governing a large bank must be men of standing and note besides, or they would discredit the bank; they need not be rich in the sense of being worth millions, but they must be known to possess a fair amount of capital and be seen to be transacting a fair quantity of business: but the labor of such persons — I do not say their spare powers, but their principal energies — fetches a high price. Business is really a profession; often requiring for its practice quite as much knowledge and quite as much skill as law and medicine, and requiring also the possession of money. A thorough man of

business, employing a fair capital in a trade which he thoroughly comprehends, not only earns a profit on that capital, but really makes of his professional skill a large income; he has a revenue from talent as well as from money: and to induce sixteen or eighteen persons to abandon such a position and such an income in order to devote their entire attention to the affairs of a joint-stock company, a salary must be given too large for the bank to pay or for any one to wish to propose.

And an effectual supervision by the whole board being impossible, there is a great risk that the whole business may fall to the general manager. Many unhappy cases have proved this to be very dangerous: even when the business of joint-stock banks was far less, and when the deposits intrusted to them were very much smaller, a manager sometimes committed frauds which were dangerous, and still oftener made mistakes that were ruinous. Actual crime will always be rare, but as an uninspected manager of a great bank has the control of untold millions, sometimes we must expect to see it: the magnitude of the temptation will occasionally prevail over the feebleness of human nature. But error is far more formidable than fraud; the mistakes of a sanguine manager are far more to be dreaded than the theft of a dishonest manager. Easy misconception is far more common than long-sighted deceit; and the losses to which an adventurous and plausible manager, in complete good faith, would readily commit a bank, are beyond comparison greater than any which a fraudulent manager would be able to conceal, even with the utmost ingenuity. If the losses by mistake in banking and the losses by fraud were put side by side, those by mistake would be incomparably the greater. There is no more unsafe government for a bank than that of an eager and active manager, subject only to the supervision of a numerous board of directors, even though that board be

excellent; for the manager may easily glide into dangerous and insecure transactions, nor can the board effectually check him.

The remedy is this: a certain number of the directors — either those who have more spare time than others, or those who are more ready to sell a large part of their time to the bank — must be formed into a real working committee, which must meet constantly, must investigate every large transaction, must be acquainted with the means and standing of every large borrower, and must be in such incessant communication with the manager that it will be impossible for him to engage in hazardous enterprises of dangerous magnitude without their knowing it and having an opportunity of forbidding it. In almost all cases they would forbid it: all committees are cautious, and a committee of careful men of business, picked from a large city, will usually err on the side of caution if it err at all. The daily attention of a small but competent minor council, to whom most of the powers of the directors are delegated, and who, like a Cabinet, guide the deliberations of the board at its meetings, is the only adequate security of a large bank from the rash engagements of a despotic and active general manager. Fraud, in the face of such a committee, would probably never be attempted; and even now it is a rare and minor evil.

Some such committees are vaguely known to exist in most if not all our large joint-stock banks: but their real constitution is not known, — no customer and no shareholder knows the names of the managing committee, perhaps, in any of these large banks; and this is a grave error. A large depositor ought to be able to ascertain who really are the persons that dispose of his money; and still more, a large shareholder ought not to rest till he knows who it is that makes engagements on his behalf, and who it is that may ruin him if they choose. The

committee ought to be composed of quiet men of business, who can be ascertained by inquiry to be of high character and well-judging mind; and if the public and the shareholder knew that there was such a committee, they would have sufficient reasons for the confidence which now is given without such reasons.

A certain number of directors attending daily by rotation is, it should be said, no substitute for a permanent committee: it has no sufficient responsibility. A changing body cannot have any responsibility: the transactions which were agreed to by one set of directors present on the Monday might be exactly those which would be much disapproved by directors present on the Wednesday. It is essential to the decisions of most business, and not least of the banking business, that they should be made constantly by the same persons; the chain of transactions must pass through the same minds. A large business may be managed tolerably by a quiet group of second-rate men, if those men be always the same; but it cannot be managed at all by a fluctuating body, even of the very cleverest men,—you might as well attempt to guide the affairs of the nation by means of a Cabinet similarly changing.

Our great joint-stock banks are imprudent in so carefully concealing the details of their government, and in secluding those details from the risk of discussion. The answer no doubt will be, "Let well alone: as you have admitted, there hardly ever before was so great a success as these banks of ours,—what more do you or can you want?" I can only say that I want further to confirm this great success, and to make it secure for the future: at present there is at least the possibility of a great reaction. Supposing that owing to defects in its government, one even of the greater London joint-stock banks failed: there would be an instant suspicion of the whole system; one *terra incognita* being seen to be

faulty, every other *terra incognita* would be suspected. If the real government of these banks had for years been known, and if the subsisting banks had been known not to be ruled by the bad mode of government which had ruined the bank that had fallen, then the ruin of that bank would not be hurtful, — the other banks would be seen to be exempt from the cause which had destroyed it; but at present the ruin of one of these great banks would greatly impair the credit of all. Scarcely any one knows the precise government of any one; in no case has that government been described on authority: and the fall of one by grave misgovernment would be taken to show that the others might as easily be misgoverned also. And a tardy disclosure even of an admirable constitution would not much help the surviving banks: as it was extracted by necessity, it would be received with suspicion; a skeptical world would say, "Of course they say they are all perfect now, — it would not do for them to say anything else."

And not only the depositors and the shareholders of these large banks have a grave interest in their good government, but the public also. We have seen that our banking reserve is, as compared with our liabilities, singularly small; we have seen that the rise of these great banks has lessened the proportion of that reserve to those liabilities; we have seen that the greatest strain on the banking reserve is a "panic." Now, no cause is more capable of producing a panic [than] — perhaps none is so capable as — the failure of a first-rate joint-stock bank in London: such an event would have something like the effect of the failure of Overend, Gurney & Co.; scarcely any other event would have an equal effect. And therefore, under the existing constitution of our banking system the government of these great banks is of primary importance to us all.

CHAPTER X.

THE PRIVATE BANKS.

Perhaps some readers of the last part of the last chapter have been inclined to say that I must be a latent enemy to joint-stock banking, — at any rate, I have pointed out what I think grave defects in it; but I fear that a reader of this chapter may, on like grounds, suppose that I am an enemy to private banking: and I can only hope that the two impressions may counteract one another, and may show that I do not intend to be unfair.

I can imagine nothing better in theory or more successful in practice than private banks as they were in the beginning. A man of known wealth, known integrity, and known ability is largely intrusted with the money of his neighbors. The confidence is strictly personal: his neighbors know him, and trust him because they know him; they see daily his manner of life, and judge from it that their confidence is deserved. In rural districts, and in former times, it was difficult for a man to ruin himself except at the place in which he lived, — for the most part he spent his money there, and speculated there if he speculated at all; those who lived there also would soon see if he was acting in a manner to shake their confidence. Even in large cities, as cities then were, it was possible for most persons to ascertain with fair certainty the real position of conspicuous persons, and to learn all which was material in fixing their credit. Accordingly, the bankers who for a long series of years passed successfully

this strict and continual investigation became very wealthy and very powerful.

The name "London banker" had especially a charmed value. He was supposed to represent, and often did represent, a certain union of pecuniary sagacity and educated refinement which was scarcely to be found in any other part of society. In a time when the trading classes were much ruder than they now are, many private bankers possessed variety of knowledge and a delicacy of attainment which would even now be very rare. Such a position is indeed singularly favorable: the calling is hereditary, the credit of the bank descends from father to son; this inherited wealth soon brings inherited refinement. Banking is a watchful but not a laborious trade: a banker even in large business can feel pretty sure that all his transactions are sound, and yet have much spare mind; a certain part of his time and a considerable part of his thoughts he can readily devote to other pursuits. And a London banker can also have the most intellectual society in the world if he chooses it. There has probably very rarely ever been so happy a position as that of a London private banker, and never perhaps a happier.

It is painful to have to doubt of the continuance of such a class, and yet I fear we must doubt of it: the evidence of figures is against it. In 1810 there were 40 private banks in Lombard Street admitted to the Clearing House, there now are only 13; though the business of banking has increased so much since 1810, this species of banks is fewer in number than it was then: nor is this the worst, — the race is not renewed. There are not many recognized impossibilities in business, but everybody admits that "you cannot found a new private bank"; no such has been founded in London, or as far as I know in the country, for many years. The old ones merge or die, and so the number is lessened; but no new ones begin so as to increase that number again.

The truth is, that the circumstances which originally favored the establishment of private banks have now almost passed away: the world has become so large and complicated that it is not easy to ascertain who is rich and who is poor. No doubt there are some enormously wealthy men in England whose means everybody has heard of and has no doubt of; but these are not the men to incur the vast liabilities of private banking. If they were bred in it they might stay in it, but they would never begin it for themselves; and if they did, I expect people would begin to doubt even of their wealth. It would be said, "What does A B go into banking for? he cannot be as rich as we thought." A millionaire commonly shrinks from liability, and the essence of great banking is great liability. No doubt there are many "second-rate" rich men, as we now count riches, who would be quite ready to add to their income the profit of a private bank, if only they could manage it; but unluckily they cannot manage it, — their wealth is not sufficiently familiar to the world, they cannot obtain the necessary confidence. No new private bank is founded in England because men of first-rate wealth will not found one, and men not of absolutely first-rate wealth cannot.

In the present day, also, private banking is exposed to a competition against which in its origin it had not to struggle: owing to the changes of which I have before spoken, joint-stock banking has begun to compete with it. In old times this was impossible, — the Bank of England had a monopoly in banking of the principle of association; but now large joint-stock banks of deposit are among the most conspicuous banks in Lombard Street. They have a large paid-up capital and intelligible published accounts; they use these as an incessant advertisement, in a manner in which no individual can use his own wealth: by their increasing progress they effectually prevent the foundation of any new private bank.

The amount of the present business of private banks is perfectly unknown, — their balance sheets are effective secrets, rigidly guarded; but none of them, except a few of the largest, are believed at all to gain business. The common repute of Lombard Street might be wrong in a particular case, but upon the general doctrine it is almost sure to be right. There are a few well-known exceptions, but according to universal belief the deposits of most private bankers in London tend rather to diminish than to increase.

As to the smaller banks, this naturally would be so, — a large bank always tends to become larger, and a small one tends to become smaller: people naturally choose for their banker the banker who has most present credit, and the one who has most money in hand is the one who possesses such credit. This is what is meant by saying that a long-established and rich bank has a "privileged opportunity": it is in a better position to do its business than any one else is; it has a great advantage over old competitors and an overwhelming superiority over newcomers. New people coming into Lombard Street judge by results: they give to those who have; they take their money to the biggest bank because it is the biggest. I confess I cannot, looking far forward into the future, expect that the smaller private banks will maintain their ground. Their old connections will not leave them; there will be no fatal ruin, no sudden mortality: but the tide will gently ebb, and the course of business will be carried elsewhere.

Sooner or later, appearances indicate and principle suggests that the business of Lombard Street will be divided between the joint-stock banks and a few large private banks; and then we have to ask ourselves the question, Can those large private banks be permanent? I am sure I should be very sorry to say that they certainly cannot; but at the same time

I cannot be blind to the grave difficulties which they must surmount.

In the first place, a hereditary business of great magnitude is dangerous: the management of such a business needs more than common industry and more than common ability, but there is no security at all that these will be regularly continued in each generation. The case of Overend, Gurney & Co., the model instance of all evil in business, is a most alarming example of this evil. No cleverer men of business, probably (cleverer, I mean, for the purposes of their particular calling), could well be found than the founders and first managers of that house; but in a very few years the rule in it passed to a generation whose folly surpassed the usual limit of imaginable incapacity,—in a short time they substituted ruin for prosperity and changed opulence into insolvency. Such great folly is happily rare, and the business of a bank is not nearly as difficult as the business of a discount company; still, much folly is common, and the business of a great bank requires a great deal of ability and an even rarer degree of trained and sober judgment. That which happened so marvelously in the green tree may happen also in the dry: a great private bank might easily become very rotten by a change from discretion to foolishness in those who conduct it.

We have had as yet in London, happily, no example of this; indeed, we have hardly as yet had the opportunity. Till now private banks have been small,—small as we now reckon banks; for their exigencies a moderate degree of ability and an anxious caution will suffice: but if the size of the banks is augmented and greater ability is required, the constant difficulty of a hereditary government will begin to be felt. "The father had great brains and created the business, but the son had less brains and lost or lessened it:" this is the history of all great monarchies, and it may be the history of great private

banks. The peculiarity in the case of Overend, Gurney & Co. — at least, one peculiarity — is, that the evil was soon discovered. The richest partners had least concern in the management; and when they found that incredible losses were ruining them, they stopped the concern and turned it into a company. But they had done nothing; if at least they had only prevented further losses, the firm might have been in existence and in the highest credit now: it was the publicity of their losses which ruined them. But if they had continued to be a private partnership they need not have disclosed those losses: they might have written them off quietly out of the immense profits they could have accumulated; they had some ten millions of other people's money in their hands which no one thought of disturbing. The perturbation through the country which their failure caused in the end, shows how diffused and how unimpaired their popular reputation was; no one in the rural districts (as I know by experience) would ever believe a word against them, say what you might. The catastrophe came because at the change the partners in the old private firm — the Gurney family especially — had guaranteed the new company against the previous losses: those losses turned out to be much greater than was expected; to pay what was necessary the Gurneys had to sell their estates, and their visible ruin destroyed the credit of the concern. But if there had been no such guaranty and no sale of estates, — if the great losses had slept a quiet sleep in a hidden ledger, — no one would have been alarmed; and the credit and the business of "Overends" might have existed till now, and their name still continued to be one of our first names. The difficulty of propagating a good management by inheritance for generations is greatest in private banks and discount firms because of their essential secrecy.

The danger may indeed be surmounted by the continual infusion of new and able partners; the

deterioration of the old blood may be compensated by the excellent quality of the fresh blood. But to this again there is an objection, of little value perhaps in seeming, but of much real influence in practice: the infusion of new partners requires from the old partners a considerable sacrifice of income; the old must give up that which the new receive, and the old will not like this. The effectual remedy is so painful that I fear it often may be postponed too long.

I cannot therefore expect with certainty the continuance of our system of private banking: I am sure that the days of small banks will before many years come to an end, and that the difficulties of large private banks are very important. In the mean time it is very important that large private banks should be well managed; and the present state of banking makes this peculiarly difficult. The detail of the business is augmenting with an overwhelming rapidity: more checks are drawn year by year, — not only more absolutely, but more by each person and more in proportion to his income; the payments in and payments out of a common account are very much more numerous than they formerly were: and this causes an enormous growth of detail. And besides, bankers have of late begun almost a new business: they now not only keep people's money, but also collect their incomes for them. Many persons live entirely on the income of shares or debentures or foreign bonds, which is paid in coupons, and these are handed in for the bank to collect; often enough the debenture or the certificate or the bond is in the custody of the banker, and he is expected to see when the coupon is due, and to cut it off and transmit it for payment: and the detail of all this is incredible, and it needs a special machinery to cope with it.

A large joint-stock bank, if well worked, has that machinery. It has at the head of the executive a

general manager who was tried in the detail of banking, who is devoted to it, and who is content to live almost wholly in it; he thinks of little else, and ought to think of little else. One of his first duties is to form a hierarchy of inferior officers, whose respective duties are defined, and to see that they can perform and do perform those duties. But a private bank of the type usual in London has no such officer. It is managed by the partners: now, these are generally rich men, are seldom able to grapple with great business of detail, and are not disposed to spend their whole lives [in] and devote their entire minds to it if they were able. A person with the accumulated wealth, the education, and the social place of a great London banker would be a fool so to devote himself: he would sacrifice a suitable and a pleasant life for an unpleasant and an unsuitable life. But still the detail must be well done; and some one must be specially chosen to watch it and to preside over it, or it will not be well done. Until now, or until lately, this difficulty has not been fully felt, — the detail of the business of a small private bank was moderate enough to be superintended effectually by the partners; but as has been said, the detail of banking — the proportion of detail to the size of the bank — is everywhere increasing. The size of the private banks will have to augment if private banks are not to cease; and therefore the necessity of a good organization for detail is urgent. If the bank grows, and simultaneously the detail grows in proportion to the bank, a frightful confusion is near unless care be taken.

The only organization which I can imagine to be effectual is that which exists in the antagonistic establishments. The great private banks will have, I believe, to appoint, in some form or other and under some name or other, some species of general manager who will watch, contrive, and arrange the

detail for them. The precise shape of the organization is immaterial, — each bank may have its own shape; but the *man* must be there. The true business of the private partners in such a bank is much that of the directors in a joint-stock bank: they should form a permanent committee to consult with their general manager, to watch him, and to attend to large loans and points of principle. They should not themselves be responsible for detail; if they do there will be two evils at once: the detail will be done badly, and the minds of those who ought to decide principal things will be distracted from those principal things. There will be a continual worry in the bank, and in a worry bad loans are apt to be made and money is apt to be lost.

A subsidiary advantage of this organization is, that it would render the transition from private banking to joint-stock banking easier, if that transition should be necessary; the one might merge in the other as convenience suggested and as events required. There is nothing intrusive in discussing this subject: the organization of the private is just like that of the joint-stock banks; all the public are interested that it should be good. The want of a good organization may cause the failure of one or more of these banks; and such failure of such banks may intensify a panic, even if it should not cause one.

CHAPTER XI.

THE BILL-BROKERS.

UNDER every system of banking — whether that in which the reserve is kept in many banks or one in which it is kept in a single bank only — there will always be a class of persons who examine more carefully than busy bankers can the nature of different securities, and who by attending only to one class come to be particularly well acquainted with that class; and as these specially qualified dealers can for the most part lend much more than their own capital, they will always be ready to borrow largely from bankers and others, and to deposit the securities which they know to be good as a pledge for the loan. They act thus as intermediaries between the borrowing public and the less qualified capitalist: knowing better than the ordinary capitalist which loans are better and which are worse, they borrow from him, and gain a profit by charging to the public more than they pay to him.

Many stock brokers transact such business upon a great scale: they lend large sums on foreign bonds or railway shares or other such securities, and borrow those sums from bankers, depositing the securities with the bankers, and generally (though not always) giving their guaranty. But by far the greatest of these intermediate dealers are the bill-brokers. Mercantile bills are an exceedingly difficult kind of security to understand. The relative credit of different merchants is a great "tradition"; it is a large mass of most valuable knowledge which has

never been described in books, and is probably incapable of being so described. The subject matter of it, too, is shifting and changing daily: an accurate representation of the trustworthiness of houses at the beginning of a year might easily be a most fatal representation at the end of it. In all years there are great changes, — some houses rise a good deal and some fall, — and in some particular years the changes are immense: in years like 1871 many active men make so much money that at the end of the year they are worthy of altogether greater credit than any one would have dreamed of giving to them at the beginning; on the other hand, in years like 1866 a contagious ruin destroys the trustworthiness of very many firms and persons, and often especially of many who stood highest immediately before. Such years alter altogether an important part of the mercantile world: the final question of bill-brokers, "Which bills will be paid and which will not? which bills are second-rate and which first-rate?" would be answered very differently at the beginning of the year and at the end. No one can be a good bill-broker who has not learnt the great mercantile tradition of what is called "the standing of parties," and who does not watch personally and incessantly the inevitable changes which from hour to hour impair the truth of that tradition. The "credit" of a person — that is, the reliance which may be placed on his pecuniary fidelity — is a different thing from his property. No doubt, other things being equal, a rich man is more likely to pay than a poor man; but on the other hand, there are many men not of much wealth who are trusted in the market, "as a matter of business," for sums much exceeding the wealth of those who are many times richer, — a firm or a person who have been long known to "meet their engagements" inspire a degree of confidence not dependent on the quantity of his or their property. Persons who buy to

sell again soon are often liable for amounts altogether much greater than their own capital; and the power of obtaining those sums depends upon their "respectability," their "standing," and their "credit," as the technical terms express it, and more simply upon the *opinion* which those who deal with them have formed of them. The principal mode in which money is raised by traders is by "bills of exchange"; the estimated certainty of their paying those bills on the day they fall due is the measure of their credit: and those who estimate that liability best — the only persons indeed who can estimate it exceedingly well — are the bill-brokers; and these dealers, taking advantage of their peculiar knowledge, borrow immense sums from bankers and others. They generally deposit the bills as a security, and they generally give their own guaranty of the goodness of the bill; but neither of such practices indeed is essential, though both are the ordinary rule. When Overends failed, as I have said before, they had borrowed in this way very largely; there are others now in the trade who have borrowed quite as much.

As is usually the case, this kind of business has grown up only gradually. In the year 1810 there was no such business precisely answering to what we now call "bill-broking" in London. Mr. Richardson, the principal bill-broker of the time, as the term was then understood, thus described his business to the "Bullion Committee":—

"What is the nature of the agency for country banks? — It is twofold: in the first place, to procure money for country bankers on bills when they have occasion to borrow on discount, which is not often the case; and in the next place, to lend the money for the country bankers on bills on discount. The sums of money which I lend for country bankers on discount are fifty times more than the sums borrowed for country bankers.

"Do you send London bills into the country for discount? — Yes.

"Do you receive bills from the country upon London in return, at a date, to be discounted? — Yes, to a very considerable amount, from particular parts of the country.

"Are not both sets of bills by this means under discount?—No, the bills received from one part of the country are sent down to another part for discount.

"And they are not discounted in London?—No. In some parts of the country there is but little circulation of bills drawn upon London, as in Norfolk, Suffolk, Essex, Sussex, etc.; but there is there a considerable circulation in country bank notes, principally optional notes. In Lancashire there is little or no circulation of country bank notes; but there is a great circulation of bills drawn upon London at two or three months' date. I receive bills to a considerable amount from Lancashire in particular, and remit them to Norfolk, Suffolk, etc., where the bankers have large lodgments and much surplus money to advance on bills for discount."

Mr. Richardson was only a broker who found money for bills and bills for money. He is further asked:—

"Do you guarantee the bills you discount, and what is your charge per cent.?—No, we do not guarantee them; our charge is one-eighth per cent. brokerage upon the bill discounted, but we make no charge to the lender of the money.

"Do you consider that brokerage as a compensation for the skill which you exercise in selecting the bills which you thus get discounted?—Yes, for selecting the bills, writing letters, and other trouble.

"Does the party who furnishes the money give you any kind of compensation?—None at all.

"Does he not consider you as his agent, and in some degree responsible for the safety of the bills which you give him?—Not at all.

"Does he not prefer you on the score of his judging that you will give him good intelligence upon that subject?—Yes, he relies upon us.

"Do you then exercise a discretion as to the probable safety of the bills?—Yes; if a bill comes to us which we conceive not to be safe, we return it.

"Do you not then conceive yourselves to depend in a great measure for the quantity of business which you can perform on the favor of the party lending the money?—Yes, very much so. If we manage our business well, we retain our friends; if we do not, we lose them."

It was natural enough that the owners of the money should not pay, though the owner of the bill

did: for in almost all ages the borrower has been a seeker more or less anxious, — he has always been ready to pay for those who will find him the money he is in search of; but the possessor of money has rarely been willing to pay anything, — he has usually and rightly believed that the borrower would discover him soon.

Notwithstanding other changes, the distribution of the customers of the bill-brokers in different parts of the country still remains much as Mr. Richardson described it sixty years ago. For the most part, agricultural counties do not employ as much money as they save; manufacturing counties, on the other hand, can employ much more than they save: and therefore the money of Norfolk or of Somersetshire is deposited with the London bill-brokers, who use it to discount the bills of Lancashire and Yorkshire.

The old practice of bill-broking, which Mr. Richardson describes, also still exists: there are many brokers to be seen about Lombard Street with bills which they wish to discount but which they do not guarantee. They have sometimes discounted these bills with their own capital: and if they can rediscount them at a slightly lower rate, they gain a difference which at first seems but trifling, but with which they are quite content, because this system of lending first and borrowing again immediately enables them to turn their capital very frequently, and on a few thousand pounds of capital to discount hundreds of thousands of bills; as the transactions are so many, they can be content with a smaller profit on each. In other cases, these non-guaranteeing brokers are only agents who are seeking money for bills which they have undertaken to get discounted. But in either case, as far as the banker or other ultimate capitalist is concerned, the transaction is essentially that which Mr. Richardson describes: the loan by such banker is a rediscount of the bill; that banker cannot

obtain repayment of that loan except by the payment of the bill at maturity, — he has no claim upon the agent who brought him the bill. Bill-broking, in this which we may call its "archaic" form, is simply one of the modes in which bankers obtain bills which are acceptable to them and which they rediscount. No reference is made in it to the credit of the bill-broker; the bills, being discounted "without recourse" to him, are as good if taken from a pauper as if taken from a millionaire: the lender exercises his own judgment on the goodness of the bill.

But in modern bill-broking the credit of the bill-broker is a vital element. The lender considers that the bill-broker — no matter whether an individual, a company, or a firm — has considerable wealth; and he takes the bills relying that the broker would not venture that wealth by guaranteeing them unless he thought them good. The lender thinks, too, that the bill-broker, being daily conversant with bills and bills only, knows probably all about bills; he lends partly in reliance on the wealth of the broker and partly in reliance on his skill. He does not exercise much judgment of his own on the bills deposited with him; he often does not watch them very closely. Probably not one-thousandth part of the creditors on security of Overend, Gurney & Co. had ever expected to have to rely on that security, or had ever given much real attention to it. Sometimes indeed the confidence in the bill-brokers goes farther: a considerable number of persons lend to them not only without much looking at the security, but even without taking any security. This is the exact reverse of the practice which Mr. Richardson described in 1810: then the lender relied wholly on the goodness of the bill; now, in these particular cases, he relies solely on the bill-broker, and does not take a bill in any shape. Nothing can be more natural or more inevitable than this change. It was certain that the bill-broker, being supposed to understand

bills well, would be asked by the lenders to evince his reliance on the bills he offered by giving a guarantee for them; it was also most natural that the bill-brokers, having by the constant practice of this lucrative trade obtained high standing and acquired great wealth, should become more or less bankers too, and should receive money on deposit without giving any security for it.

But the effects of the change have been very remarkable. In the practice as Mr. Richardson described it, there is no peculiarity very likely to affect the money market: the bill-broker brought bills to the banker, just as others brought them; nothing at all could be said as to it except that the bank must not discount bad bills, must not discount too many bills, and must keep a good reserve. But the modern practice introduces more complex considerations. In the trade of bill-broking as it now exists there is one great difficulty: the bill-broker has to pay interest for all the money which he receives. How this arose we have just seen: the present lender to the bill-broker at first always used to discount a bill, which is as much as saying that he was always a lender at interest; when he came to take the guarantee of the broker, and only to look at the bills as a collateral security, naturally he did not forego his interest, — still less did he forego it when he ceased to take security at all. The bill-broker has, in one shape or other, to pay interest on every sixpence left with him; and that constant habit of giving interest has this grave consequence, — the bill-broker cannot afford to keep much money unemployed. He has become a banker, owing large sums which he may be called on to repay; but he cannot hold as much as an ordinary banker, or nearly as much, of such sums in cash, because the loss of interest would ruin him. Competition reduces the rate which the bill-broker can charge and raises the rate which the bill-broker must give, so that he has to live on a difference

exceedingly narrow; and if he constantly kept a large hoard of barren money, he would soon be found in the *Gazette*.

The difficulty is aggravated by the terms upon which a great part of the money at the bill-brokers is deposited with them: very much of it is repayable at demand or at very short notice; the demands on a broker in periods of alarm may consequently be very great, and in practice they often are so. In times of panic there is always a very heavy call, if not a run, upon them; and [as] in consequence of the essential nature of their business they cannot constantly keep a large unemployed reserve of their own in actual cash, they are obliged to ask help of some one who possesses that cash. . By the conditions of his trade the bill-broker is forced to belong to a class of "dependent money dealers," as we may term them; that is, of dealers who do not keep their own reserve, and must therefore at every crisis of great difficulty revert to others.

In a natural state of banking — that in which all the principal banks kept their own reserve — this demand of the bill-brokers and other dependent dealers would be one of the principal calls on that reserve. At every period of incipient panic, the holders of it would perceive that it was of great importance to themselves to support these dependent dealers: if the panic destroyed those dealers, it would grow by what it fed upon (as is its nature), and might probably destroy also the bankers, the holders of the reserve. The public terror at such times is indiscriminate: when one house of good credit has perished, other houses of equal credit though of different nature are in danger of perishing. The many holders of the banking reserve would under the natural system of banking be obliged to advance out of that reserve to uphold bill-brokers and similar dealers; it would be essential to their own preservation not to let such dealers fail, and the protection of

such dealers would therefore be reckoned among the necessary purposes for which they retained that reserve.

Nor probably would the demands on the bill-brokers in such a system of banking be exceedingly formidable. Considerable sums would no doubt be drawn from them, but there would be no special reason why money should be demanded from them more than from any other money dealers; they would share the panic with the bankers who kept the reserve, but they would not feel it more than the bankers. In each crisis the set of the storm would be determined by the cause which had excited it, but there would not be anything in the nature of bill-broking to attract the advance of the alarm peculiarly to them, — they would not be more likely to suffer than other persons; the only difference would be that when they did suffer, having no adequate reserve of their own, they would be obliged to ask the aid of others.

But under a *one*-reserve system of banking, the position of the bill-brokers is much more singular and much more precarious. In fact, in Lombard Street, the principal depositors of the bill-brokers are the bankers, whether of London or of provincial England or of Scotland or Ireland. Such deposits are in fact a portion of the reserve of these bankers; they make an essential part of the sums which they have provided and laid by against a panic: accordingly, in every panic these sums are sure to be called in from the bill-brokers; they were wanted to be used by their owners in time of panic, and in time of panic they ask for them. "Perhaps it may be interesting to the Committee," said Alderman Salomons, speaking on behalf of the London and Westminster Bank, after the panic of 1857, "to know that on the 11th of November we held discounted bills for brokers to the amount of £5,623,000; out of those bills £2,800,000 matured between the 11th of November and the 4th of December, and £2,000,000 more

between the 4th of December and the 31st: consequently we were prepared, merely by the maturing of our bills of exchange, for any demand that might come upon us." * This is not indeed a direct withdrawal of money on deposit, but its principal effect is identical: at the beginning of the time the London and Westminster Bank had lent £5,000,000 more to the bill-brokers than they had at the end of it, and that £5,000,000 the bank had added to its reserve against a time of difficulty.

The intensity of the demand on the bill-broker[s] is aggravated, therefore, by our peculiar system of banking: just at the moment when, by the nature of their business, they have to resort to the reserves of bankers for necessary support, the bankers remove from them large sums in order to strengthen those reserves. A great additional strain is thrown upon them just at the moment when they are least able to bear it; and it is thrown by those who under a natural system of banking would not aggravate the pressure on the bill-brokers, but relieve it.

And the profits of bill-broking are proportionably raised. The reserves of the bankers so deposited with the bill-broker form a most profitable part of his business: they are on the whole of very large amount, and at all times except those of panic may well be depended upon, — the bankers are pretty sure to keep them there, just because they must keep a reserve and they consider it one of the best places in which to keep it. Under a more natural system, no part of the banking reserve would ever be lodged at the brokers: bankers would deposit with the brokers only their extra money, — the money which they considered they could safely lend, and which they would not require during a panic; in the eye of the banker, money at the brokers would then be one of the investments of cash, it would not be a part of such cash. The deposits of bill-brokers and the profits

* See Note B, Appendix.

of bill-broking are increased by our present system, just in proportion as the dangers of bill-brokers during a panic are increased by it.

The strain, too, on our banking reserve which is caused by the demands of the bill-brokers, is also more dangerous than it would be under a natural system, because that reserve is in itself less. The system of keeping the entire ultimate reserve at a single bank, undoubtedly diminishes the amount of reserve which is kept; and exactly on that very account the danger of any particular demand on that reserve is augmented, because the magnitude of the fund upon which that demand falls is diminished. So that our one-reserve system of banking combines two evils: first, it makes the demand of the brokers upon the final reserve greater, because under it so many bankers remove so much money from the brokers; and under it also the final reserve is reduced to its minimum point, and the entire system of credit is made more delicate and more sensitive.

The peculiarity, indeed, of the effects of the one reserve is indeed even greater in this respect. Under the natural system, the bill-brokers would be in no respect the rivals of the bankers which kept the ultimate reserve; they would be rather the agents for these bankers in lending upon certain securities which they did not themselves like, or on which they did not feel competent to lend safely: the bankers who in time of panic had to help them would in ordinary times derive much advantage from them. But under our present system all this is reversed. The Bank of England never deposits any money with the bill-brokers; in ordinary times it never derives any advantage from them. On the other hand, as the Bank carries on itself a large discount business, as it considers that it is itself competent to lend on all kinds of bills, the bill-brokers are its most formidable rivals: as they constantly give high rates for money, it is necessary that they should undersell

the Bank, and in ordinary times they do undersell it. But as the Bank of England alone keeps the final banking reserve, the bill-brokers of necessity have to resort to that final reserve; so that at every panic, and by the essential constitution of the money market, the Bank of England has to help, has to maintain in existence, the dealers who never in return help the Bank at any time, but who are in ordinary times its closest competitors and its keenest rivals.

It might be expected that such a state of things would cause much discontent at the Bank of England; and in matter of fact there has been much discussion about it and much objection taken to it. After the panic of 1857 this was so especially: during that panic the Bank of England advanced to the bill-brokers more than £9,000,000, though their advances to bankers, whether London or country, were only £8,000,000; and not unnaturally, the Bank thought it unreasonable that so large an inroad upon their resources should be made by their rivals. In consequence, in 1858 they made a rule that they would only advance to the bill-brokers at certain seasons of the year, when the public money is particularly large at the Bank, and that at other times any application for an advance should be considered exceptional, and dealt with accordingly; and the object of that regulation was officially stated to be "to make them keep their own reserve, and not to be dependent on the Bank of England." As might be supposed, this rule was exceedingly unpopular with the brokers; and the greatest of them, Overend, Gurney & Co., resolved on a strange policy in the hope of abolishing it. They thought they could frighten the Bank of England, and could show that if they were dependent on it, it was also dependent on them; they accordingly accumulated a large deposit at the Bank, to the amount of £3,000,000, and then withdrew it all at once. But this policy had no effect except that of exciting a distrust of "Overends": the credit of the

Bank of England was not diminished; Overends had to return the money in a few days, and had the dissatisfaction of feeling that they had in vain attempted to assail the solid basis of every one's credit, and that every one disliked them for doing so. But though this ill-conceived attempt failed as it deserved, the rule itself could not be maintained: the Bank does in fact, at every period of pressure, advance to the bill-brokers; the case may be considered "exceptional," but the advance is always made if the security offered is really good. However much the Bank may dislike to aid their rivals, yet they must aid them: at a crisis they feel that they would only be aggravating incipient demand and be augmenting the probable pressure on themselves if they refused to do so.

I shall be asked if this anomaly is inevitable; and I am afraid that for practical purposes we must consider it to be so. It may be lessened: the bill-brokers may and should discourage as much as they can the deposit of money with them on demand, and encourage the deposit of it at distant fixed dates or long notice; this will diminish the anomaly, but it will not cure it. Practically, bill-brokers cannot refuse to receive money at call: in every market a dealer must conduct his business according to the custom of the market, or he will not be able to conduct it at all. All the bill-brokers can do is to offer better rates for more permanent money; and this (though possibly not so much as might be wished) they do at present. In its essence, this anomaly is, I believe, an inevitable part of the system of banking which history has given us, and which we have only to make the best of, since we cannot alter it.

CHAPTER XII.

THE PRINCIPLES WHICH SHOULD REGULATE THE AMOUNT OF THE BANKING RESERVE TO BE KEPT BY THE BANK OF ENGLAND.

THERE is a very common notion that the amount of the reserve which the Bank of England ought to keep can be determined at once from the face of their weekly balance sheet; it is imagined that you have only to take the liabilities of the Banking Department, and that a third or some other fixed proportion will in all cases be the amount of reserve which the Bank should keep against those liabilities: but to this there are several objections, some arising from the general nature of the banking trade, and others from the special position of the Bank of England.

That the amount of the liabilities of a bank is a principal element in determining the proper amount of its reserve, is plainly true; but that it is the only element by which that amount is determined, is plainly false,—the intrinsic nature of these liabilities must be considered, as well as their numerical quantity. For example, no one would say that the same amount of reserve ought to be kept against acceptances which cannot be paid except at a certain day, and against deposits at call, which may be demanded at any moment: if a bank groups these liabilities together in the balance sheet, you cannot tell the amount of reserve it ought to keep,—the necessary information is not given you.

Nor can you certainly determine the amount of reserve necessary to be kept against deposits unless

you know something as to the nature of these deposits. If out of £3,000,000 of money, one depositor has £1,000,000 to his credit and may draw it out when he pleases, a much larger reserve will be necessary against that liability of £1,000,000 than against the remaining £2,000,000: the *intensity* of the liability, so to say, is much greater, and therefore the provision in store must be much greater also. On the other hand, supposing that this single depositor is one of calculable habits, — suppose that it is a public body, the time of whose demands is known and the time of whose receipts is known also, — this single liability requires a less reserve than that of an equal amount of ordinary liabilities: the danger that it will be called for is much less, and therefore the security taken against it may be much less too. Unless the quality of the liabilities is considered as well as their quantity, the due provision for their payment cannot be determined.

These are general truths as to all banks, and they have a very particular application to the Bank of England. The first application is favorable to the Bank; for it shows the danger of one of the principal liabilities to be much smaller than it seems. The largest account at the Bank of England is that of the English government; and probably there has never been any account of which it was so easy in time of peace to calculate the course. All the material facts relative to the English revenue and the English expenditure are exceedingly well known; and the amount of the coming payments to and from this account are always, except in war times, to be calculated with wonderful accuracy. In war, no doubt, this is all reversed: the account of a government at war is probably the most uncertain of all accounts, especially of a government of a scattered empire like the English, whose places of outlay in time of war are so many and so distant, and the amount of whose payments is therefore so incalculable.

Ordinarily, however, there is no account of which the course can be so easily predicted, and therefore no account which needs in ordinary times so little reserve. The principal payments, when they are made, are also of the most satisfactory kind to a banker: they are to a great extent made to another account at his bank. These largest ordinary payments of the government are the dividends on the debt, and these are mostly made to bankers who act as agents for the creditors of the nation. The payment of the dividends for the government is therefore in great part a transfer from the account of the government to the accounts of the various bankers. A certain amount, no doubt, goes almost at once to the non-banking classes,— to those who keep coin and notes in house, and have no account at any bank; but even this amount is calculable, for it is always nearly the same: and the entire operation is, to those who can watch it, singularly invariable time after time.

But it is important to observe that the published accounts of the Bank give no such information to the public as will enable them to make their own calculations. The account of which we have been speaking is the yearly account of the English government, — what we may call the Budget account, that of revenue and expenditure, — and the laws of this are, as we have shown, already known; but under the head "Public Deposits" in the accounts of the Bank are contained also other accounts, and particularly that of the Secretary for India in Council, the laws of which must be different and are quite unknown. The Secretary for India is a large lender on its account. If any one proposed to give such power to the Chancellor of the Exchequer, there would be great fear and outcry; but so much depends on habit and tradition that the India Office on one side of Downing Street can do without remark, and with universal assent, what it would be thought "unsound" and extravagant to propose that the other

side should do. The present India Office inherits this independence from the old board of the company, which, being mercantile and business-like, used to lend its own money on the Stock Exchange as it pleased; the Council of India, its successor, retains the power. Nothing can be better than that it should be allowed to do as it likes; but the mixing up the account of a body which has such a power, and which draws money from India, with that of the Home government, clearly prevents the general public from being able to draw inferences as to the course of the combined account from its knowledge of home finance only. The account of "public deposits" in the Bank return includes other accounts too, as the Savings Bank balance, the Chancery Funds account, and others; and in consequence, till lately the public had but little knowledge of the real changes of the account of our government, properly so called. But Mr. Lowe has lately given us a weekly account; and from this, and not from the Bank account, we are able to form a judgment. This account and the return of the Bank of England, it is true, unhappily appear on different days; but except for that accident our knowledge would be perfect, and as it is, for almost all purposes what we know is reasonably sufficient, — we can now calculate the course of the government account nearly as well as it is possible to calculate it.

So far, as we have said, an analysis of the return of the Bank of England is very favorable to the Bank: so great a reserve need not usually be kept against the government account as if it were a common account. We know the laws of its changes peculiarly well: we can tell when its principal changes will happen with great accuracy: and we know that at such changes most of what is paid away by the government is only paid to other depositors at the Bank, and that it will really stay at the Bank, though under another name. If we look

to the private deposits of the Bank of England, at first sight we may think that the result is the same. By far the most important of these are the bankers' deposits; and for the most part, these deposits as a whole are likely to vary very little. Each banker, we will suppose, keeps as little as he can; but in all domestic transactions, payment from one is really payment to the other. All the most important transactions in the country are settled by checks; these checks are paid in to the Clearing House, and the balances resulting from them are settled by transfers from the account of one banker to another at the Bank of England. Payments out of the bankers' balances, therefore, correspond with payments in; as a whole, the deposit of the bankers' balances at the Bank of England would at first sight seem to be a deposit singularly stable.

Indeed, they would seem, so to say, to be better than stable: they augment when everything else tends to diminish. At a panic, when all other deposits are likely to be taken away, the bankers' deposits augment; in fact they did so in 1866, though we do not know the particulars: and it is natural that they should so increase. At such moments all bankers are extremely anxious, and they try to strengthen themselves by every means in their power; they try to have as much money as it is possible at command; they augment their reserve as much as they can, and they place that reserve at the Bank of England. A deposit which is not likely to vary in ordinary times, and which is likely to augment in times of danger, seems in some sort the model of a deposit; it might seem not only that a large proportion of it might be lent, but that the whole of it might be so. But a further analysis will, as I believe, show that this conclusion is entirely false; that the bankers' deposits are a singularly treacherous form of liability; that the utmost caution ought to be used in dealing with them; that as a rule, a less proportion of them ought to be lent than of ordinary deposits.

The easiest mode of explaining anything is usually to exemplify it by a single actual case; and in this subject, fortunately, there is a most conspicuous case near at hand. The German government has lately taken large sums in bullion from this country, in part from the Bank of England and in part not, according as it chose. It was in the main well advised and considerate in its action, and did not take nearly as much from the Bank as it might, or as would have been dangerous; still, it took large sums from the Bank, and it might easily have taken more. How then did the German government obtain this vast power over the Bank? The answer is, that it obtained it by means of the bankers' balances, and that it did so in two ways.

First, the German government had a large balance of its own lying at a particular joint-stock bank. That bank lent this balance at its own discretion, to bill-brokers or others, and it formed a single item in the general funds of the London market. There was nothing special about it, except that it belonged to a foreign government, and that its owner was always likely to call it in and sometimes did so. As long as it stayed unlent in the London Joint-Stock Bank, it increased the balances of that bank at the Bank of England; but so soon as it was lent, say, to a bill-broker, it increased the bill-broker's balance; and as soon as it was employed by the bill-broker in the discount of bills, the owners of those bills paid it to their credit at their separate banks, and it augmented the balances of those bankers at the Bank of England. Of course if it were employed in the discount of bills belonging to foreigners, the money might be taken abroad, and by similar operations it might also be transferred to the English provinces or to Scotland: but as a rule such money, when deposited in London, for a considerable time remains in London; and so long as it does so, it swells the aggregate balances of the body of bankers

at the Bank of England. It is now in the balance of one bank, now of another, but it is always dispersed about those balances somewhere. The evident consequence is, that this part of the bankers' balances is at the mercy of the German government when it chooses to apply for it. Supposing, then, the sum to be three or four millions, — and I believe that on more than one occasion in the last year or two it has been quite as much, if not more, — that sum might at once be withdrawn from the Bank of England. In this case the Bank of England is in the position of a banker who is liable for a large amount to a single customer, but with this addition, that it is liable for an *unknown* amount. The German government, as is well known, keeps its account (and a very valuable one it must be) at the London Joint-Stock Bank; but the Bank of England has no access to the account of the German government at that bank, — they cannot tell how much German money is lying to the credit there. Nor can the Bank of England infer much from the balance of the London Joint-Stock Bank in their Bank, for the German money was probably paid in various sums to that bank, and lent out again in other various sums: it might to some extent augment that bank's balance at the Bank of England, or it might not, but it certainly would not be so much added to that balance; and inspection of that bank's balance would not enable the Bank of England to determine even in the vaguest manner what the entire sum was for which it might be asked at any moment. Nor would the inspection of the bankers' balances as a whole lead to any certain and sure conclusions; something might be inferred from them, but not anything certain. Those balances are no doubt in a state of constant fluctuation; and very possibly during the time that the German money was coming in, some other might be going out. Any sudden increase in the bankers' balances would be a probable indication of new for-

eign money; but new foreign money might come in without causing an increase, since some other and contemporaneous cause might effect a counteracting decrease.

This is the first and the plainest way in which the German government could take and did take money from this country, and in which it might have broken the Bank of England if it had liked; the German government had money here and took it away, which is very easy to understand. But the government also possessed a far greater power, of a somewhat more complex kind: it was the owner of many debts from England. A large part of the "indemnity" was paid by France to Germany in bills on England; and the German government, as those bills came due, acquired an unprecedented command over the market. As each bill arrived at maturity, the German government could, if it chose, take the proceeds abroad; and it could do so in bullion, as for coinage purposes it wanted bullion. This would at first naturally cause a reduction in the bankers' balances; at least that would be its tendency. Supposing the German government to hold bill A, a good bill, the banker at whose bank bill A was payable would have to pay it, and that would reduce *his* balance; and as the sum so paid would go to Germany, it would not appear to the credit of any other banker: the aggregate of the bankers' balances would thus be reduced. But this reduction would not be permanent. A banker who has to pay £100,000 cannot afford to reduce his balance at the Bank of England £100,000: suppose that his liabilities are £2,000,000, and that as a rule he finds it necessary to keep at the Bank one-tenth of these liabilities, or £200,000, the payment of £100,000 would reduce his reserve to £100,000; but his liabilities would be still £1,900,000, and therefore to keep up his tenth he would have £90,000 to find. His process for finding it is this: he calls in, say, a loan to the bill-brokers; and if no equal additional

money is contemporaneously carried to these brokers (which in the case of a large withdrawal of foreign money is not probable), they must reduce their business and discount less. But the effect of this is, to throw additional business on the Bank of England: they hold the ultimate reserve of the country, and they must discount out of it if no one else will; if they declined to do so, there would be panic and collapse. As soon therefore as the withdrawal of the German money reduces the bankers' balances, there is a new demand on the Bank for fresh discounts to make up those balances. The drain on the Bank is twofold: first the banking reserve is reduced by exportation of the German money, which reduces the means of the Bank of England; and then out of those reduced means the Bank of England has to make greater advances.

The same result may be arrived at more easily. Supposing any foreign government or person to have any sort of securities which he can pledge in the market, that operation gives it or him a credit on some banker, and enables it or him to take money from the banking reserve at the Bank of England, and from the bankers' balances; and to replace the bankers' balances at their inevitable minimum, the Bank of England must lend. Every sudden demand on the country causes, in proportion to its magnitude, this peculiar effect. And this is the reason why the Bank of England ought, I think, to deal most cautiously and delicately with their banking deposits: they are the symbol of an indefinite liability; by means of them, as we see, an amount of money so great that it is impossible to assign a limit to it might be abstracted from the Bank of England. As the Bank of England lends money to keep up the bankers' balances at their usual amount, and as by means of that usual amount whatever sum foreigners can get credit for may be taken from us, it is not possible to assign a superior limit (to use the

scientific word) to the demands which by means of the bankers' balances may be made upon the Bank of England.

The result comes round to the simple point, on which this book is a commentary: the Bank of England, by the effect of a long history, holds the ultimate cash reserve of the country; whatever cash the country has to pay comes out of that reserve, and therefore the Bank of England has to pay it. And it is as the bankers' Bank that the Bank of England has to pay it, for it is by being so that it becomes the keeper of the final cash reserve.

Some persons have been so much impressed with such considerations as these, that they have contended that the Bank of England ought never to lend the "bankers' balances" at all; that they ought to keep them intact and as an unused deposit. I am not sure indeed that I have seen that extreme form of the opinion in print, but I have often heard it in Lombard Street, from persons very influential and very qualified to judge; even in print I have seen close approximations to it. But I am satisfied that the laying down such a "hard and fast" rule would be very dangerous: in very important and very changeable business, rigid rules are apt to be often dangerous. In a panic, as has been said, the bankers' balances greatly augment. It is true, the Bank of England has to lend the money by which they are filled: the banker calls in his money from the bill-broker, ceases to rediscount for that broker, or borrows on securities, or sells securities; and in one or other of these ways he causes a new demand for money, which can only at such times be met from the Bank of England, — every one else is in want too. But without inquiring into the origin of the increase at panics, the amount of the bankers' deposits in fact increases very rapidly; an immense amount of unused money is at such moments often poured by them into the Bank of England: and nothing can more

surely aggravate the panic than to forbid the Bank of England to lend that money. Just when money is most scarce, you happen to have an unusually large fund of this particular species of money; and you should lend it as fast as you can at such moments, for it is ready lending which cures panics, and non-lending or niggardly lending which aggravates them.

At other times, particularly at the quarterly payment of the dividends, an absolute rule which laid down that the bankers' balances were never to be lent would be productive of great inconvenience. A large sum is just then paid from the government balance to the bankers' balances; and if you permitted the Bank to lend it while it was still in the hands of the government, but forbade them to lend it when it came into the hands of the bankers, a great tilt upwards in the value of money would be the consequence, for a most important amount of it would suddenly have become ineffective.

But the idea that the bankers' balances ought never to be lent is only a natural aggravation of the truth that these balances ought to be used with extreme caution; that as they entail a liability peculiarly great and singularly difficult to foresee, they ought never to be used like a common deposit.

It follows from what has been said, that there are always possible and very heavy demands on the Bank of England which are not shown in the account of the Banking Department at all: these demands may be greatest when the liabilities shown by that account are smallest, and lowest when those liabilities are largest. If, for example, the German government brings bills or other good securities to this market, obtains money with them, and removes that money from the market in bullion, that money may, if the German government choose, be taken wholly from the Bank of England. If the wants of the German government be urgent, and if the amount of gold "arrivals"—that is, the gold coming here from the

mining countries — be but small, that gold will be taken from the Bank of England, for there is no other large store in the country. The German government is only a conspicuous example of a foreign power which happens lately to have had an unusual command of good securities, and an unusually continuous wish to use them in England. Any foreign state hereafter which wants cash will be likely to come here for it; so long as the Bank of France should continue not to pay in specie, a foreign state which wants it must of necessity come to London for it: and no indication of the likelihood or unlikelihood of that want can be found in the books of the Bank of England.

What is almost a revolution in the policy of the Bank of England necessarily follows: no certain or fixed proportion of its liabilities can in the present times be laid down as that which the Bank ought to keep in reserve. The old notion that one-third, or any other such fraction, is in all cases enough, must be abandoned: the probable demands upon the Bank are so various in amount, and so little disclosed by the figures of the account, that no simple and easy calculation is a sufficient guide; a definite proportion of the liabilities might often be too small for the reserve, and sometimes too great. The forces of the enemy being variable, those of the defense cannot always be the same.

I admit that this conclusion is very inconvenient. In past times it has been a great aid to the Bank and to the public to be able to decide on the proper policy of the Bank from a mere inspection of its account; in that way the Bank knew easily what to do, and the public knew easily what to foresee. But unhappily, the rule which is most simple is not always the rule which is most to be relied upon. The practical difficulties of life often cannot be met by very simple rules: those dangers being complex and many, the rules for encountering them cannot well

be single or simple. A uniform remedy for many diseases often ends by killing the patient.

Another simple rule often laid down for the management of the Bank of England must now be abandoned also: it has been said that the Bank of England should look to the market rate, and make its own rate conform to that. This rule was indeed always erroneous, — the first duty of the Bank of England was to protect the ultimate cash of the country, and to raise the rate of interest so as to protect it; but this rule was never so erroneous as now, because the number of sudden demands upon that reserve was never formerly so great. The market rate of Lombard Street is not influenced by those demands; that rate is determined by the amount of deposits in the hands of bill-brokers and bankers, and the amount of good bills and acceptable securities offered at the moment. The probable efflux of bullion from the Bank scarcely affects it at all; even the real efflux affects it but little: if the open market did not believe that the Bank rate would be altered in consequence of such effluxes, the market rate would not rise. If the Bank choose to let its bullion go unheeded, and is seen to be going so to choose, the value of money in Lombard Street will remain unaltered. The more numerous the demands on the Bank for bullion, and the more variable their magnitude, the more dangerous is the rule that the Bank rate of discount should conform to the market rate. In former quiet times, the influence or the partial influence of that rule has often produced grave disasters; in the present difficult times, an adherence to it is a *recipe* for making a large number of panics.

A more distinct view of abstract principle must be taken before we can fix on the amount of the reserve which the Bank of England ought to keep. Why should a bank keep any reserve? Because it may be called on to pay certain liabilities at once and in a moment. Why does any bank publish an

account? In order to satisfy the public that it possesses cash or available securities enough to meet its liabilities. The object of publishing the account of the Banking Department of the Bank of England is to let the nation see how the national reserve of cash stands, — to assure the public that there is enough and more than enough to meet not only all probable calls, but all calls of which there can be a chance of reasonable apprehension; and there is no doubt that the publication of the Bank account gives more stability to the money market than any other kind of precaution would give. Some persons, indeed, feared that the opposite result would happen; they feared that the constant publication of the incessant changes in the reserve would terrify and harass the public mind. An old banker once told me: — "Sir, I was on Lord Althorp's committee which decided on the publication of the Bank account, and I voted against it, — I thought it would frighten people; but I am bound to own that the committee was right and I was wrong, for that publication has given the money market a greater sense of security than anything else which has happened in my time." The diffusion of confidence through Lombard Street and the world is the object of the publication of the Bank accounts and of the Bank reserve.

But that object is not attained if the amount of that reserve when so published is not enough to tranquilize people; a panic is sure to be caused if that reserve is, from whatever cause, exceedingly low. At every moment there is a certain minimum which I will call the "apprehension minimum," below which the reserve cannot fall without great risk of diffused fear; and by this I do not mean absolute panic, but only a vague fright and timorousness which spreads itself instantly, and as if by magic, over the public mind. Such seasons of incipient alarm are exceedingly dangerous, because they beget the calamities they dread.* What is most feared

* These two words should read, "that are dreaded." — Ed.

at such moments of susceptibility is the destruction of credit; and if any grave failure or bad event happens at such moments, the public fancy seizes on it, there is a general run, and credit is suspended. The Bank reserve, then, never ought to be diminished below the "apprehension point": and this is as much as to say that it never ought very closely to approach that point; since if it gets very near, some accident may easily bring it down to that point and cause the evil that is feared.

There is no "royal road" to the amount of the "apprehension minimum": no abstract argument and no mathematical computation will teach it to us; and we cannot expect that they should. Credit is an opinion generated by circumstances and varying with those circumstances. The state of credit at any particular time is a matter of fact, only to be ascertained like other matters of fact; it can only be known by trial and inquiry. And in the same way, nothing but experience can tell us what amount of "reserve" will create a diffused confidence; on such a subject there is no way of arriving at a just conclusion except by incessantly watching the public mind, and seeing at each juncture how it is affected.

Of course in such a matter the cardinal rule to be observed is, that errors of excess are innocuous but errors of defect are destructive: too much reserve only means a small loss of profit, but too small a reserve may mean ruin; credit may be at once shaken, and if some terrifying accident happen to supervene, there may be a run on the Banking Department that may be too much for it, as in 1857 and 1866, and may make it unable to pay its way without assistance, as it was in those years.

And the observance of this maxim is the more necessary because the "apprehension minimum" is not always the same; on the contrary, in times when the public has recently seen the Bank of England exposed to remarkable demands, it is likely to expect

that such demands may come again. Conspicuous and recent events educate it, so to speak; it expects that much will be demanded when much has of late often been demanded, and that little will be so when in general but little has been so. A bank like the Bank of England must always, therefore, be on the watch for a rise, if I may so express it, in the "apprehension minimum": it must provide an adequate fund not only to allay the misgivings of to-day, but also to allay what may be the still greater misgivings of to-morrow; and the only practical mode of obtaining this object is to keep the actual reserve always in advance of the minimum "apprehension" reserve.

And this involves something much more: as the actual reserve is never to be less [than], and is always if possible to exceed by a reasonable amount, the minimum "apprehension" reserve, it must, when the Bank is quiet and taking no precautions, very considerably exceed that minimum. All the precautions of the Bank take time to operate. The principal precaution is a rise in the rate of discount, and such a rise certainly does attract money from the Continent and from all the world much faster than could have been anticipated: but it does not act instantaneously; even the right rate, the ultimately attractive rate, requires an interval for its action, and before the money can come here. And the right rate is often not discovered for some time: it requires several "moves," as the phrase goes, — several augmentations of the rate of discount by the Bank, — before the really effectual rate is reached; and in the mean time bullion is ebbing away and the reserve is diminishing. Unless, therefore, in times without precaution the actual reserve exceed the "apprehension minimum" by at least the amount which may be taken away in the inevitable interval, and before the available precautions begin to operate, the rule prescribed will be infringed, and the actual reserve will

be less than the "apprehension" minimum. In time the precautions taken may attract gold and raise the reserve to the needful amount; but in the interim the evils may happen against which the rule was devised,—diffused apprehension may arise, and then any unlucky accident may cause many calamities.

I may be asked, "What does all this reasoning in practice come to? At the present moment how much reserve do you say the Bank of England should keep? State your recommendation clearly" (I know it will be said) "if you wish to have it attended to." And I will answer the question plainly, though in so doing there is a great risk that the principles I advocate may be in some degree injured through some mistake I may make in applying them.

I should say that at the present time, the mind of the monetary world would become feverish and fearful if the reserve in the Banking Department of the Bank of England went below £10,000,000. Estimated by the idea of old times, by the idea even of ten years ago, that sum I know sounds extremely large. My own nerves were educated to smaller figures; because I was trained in times when the demands on us were less, when neither was so much reserve wanted nor did the public expect so much. But I judge from such observations as I can make of the present state of men's minds, that in fact, and whether justifiably or not, the important and intelligent part of the public which watches the Bank reserve becomes anxious and dissatisfied if that reserve falls below £10,000,000; that sum, therefore, I call the "apprehension minimum" for the present times. Circumstances may change and may make it less or more; but according to the most careful estimate I can make, that is what I should call it now.

It will be said that this estimate is arbitrary and these figures are conjectures: I reply that I only submit them for the judgment of others. The main question is one of fact: Does not the public

mind begin to be anxious and timorous just where I have placed the apprehension point? and the deductions from that are comparatively simple questions of mixed fact and reasoning. The final appeal in such cases necessarily is to those who are conversant with and who closely watch the facts.

I shall perhaps be told also that a body like the Court of the Directors of the Bank of England cannot act on estimates like these; that such a body must have a plain rule and keep to it. I say in reply that if the correct framing of such estimates is necessary for the good guidance of the Bank, we must make a governing body which can correctly frame such estimates; we must not suffer from a dangerous policy because we have inherited an imperfect form of administration. I have before explained in what manner the government of the Bank of England should, I consider, be strengthened; and that government so strengthened would, I believe, be altogether competent to a wise policy.

Then I should say, putting the foregoing reasoning into figures, that the Bank ought never to keep less than £11,000,000 or £11,500,000; since experience shows that a million, or a million and a half, may be taken from us at any time. I should regard this as the practical minimum at which, roughly of course, the Bank should aim, and which it should try never to be below. And in order not to be below £11,500,000, the Bank must begin to take precautions when the reserve is between £14,000,000 and £15,000,000; for experience shows that between £2,000,000 and £3,000,000 may, probably enough, be withdrawn from the Bank store before the right rate of interest is found which will attract money from abroad, and before that rate has had time to attract it. When the reserve is between £14,000,000 and £15,000,000, and when it begins to be diminished by foreign demand, the Bank of England should, I think, begin to act and to raise the rate of interest.

CHAPTER XIII.

CONCLUSION.

I KNOW it will be said that in this work I have pointed out a deep malady, and only suggested a superficial remedy. I have tediously insisted that the natural system of banking is that of many banks keeping their own cash reserve, with the penalty of failure before them if they neglect it; I have shown that our system is that of a single bank keeping the whole reserve, under no effectual penalty of failure: and yet I propose to retain that system, and only attempt to mend and palliate it.

I can only reply that I propose to retain this system because I am quite sure that it is of no manner of use proposing to alter it. A system of credit which has slowly grown up as years went on, which has suited itself to the course of business, which has forced itself on the habits of men, will not be altered because theorists disapprove of it or because books are written against it. You might as well, or better, try to alter the English monarchy and substitute a republic, as to alter the present constitution of the English money market, founded on the Bank of England, and substitute for it a system in which each bank shall keep its own reserve. There is no force to be found adequate to so vast a reconstruction and so vast a destruction, and therefore it is useless proposing them.

No one who has not long considered the subject can have a notion how much this dependence on the Bank of England is fixed in our national habits. I have given so many illustrations in this book that

I fear I must have exhausted my readers' patience; but I will risk giving another. I suppose almost every one thinks that our system of savings banks is sound and good; almost every one would be surprised to hear that there is any possible objection to it: yet see what it amounts to. By the last return the savings banks — the old and the Post Office together — contain about £60,000,000 of deposits, and against this they hold in the funds, securities of the best kind; but they hold no cash whatever. They have of course the petty cash about the various branches necessary for daily work; but of cash in ultimate reserve — cash in reserve against a panic — the savings banks have not a sixpence. These banks depend on being able in a panic to realize their securities; but it has been shown over and over again that in a panic such securities can only be realized by the help of the Bank of England, — that it is only the Bank with the ultimate cash reserve which has at such moments any new money, or any power to lend and act. If in a general panic there were a run on the savings banks, those banks could not sell £100,000 of consols without the help of the Bank of England; not holding themselves a cash reserve for times of panic, they are entirely dependent on the one Bank which does hold that reserve.

This is only a single additional instance, beyond the innumerable ones given, which shows how deeply our system of banking is fixed in our ways of thinking: the government keeps the money of the poor upon it, and the nation fully approves of their doing so; no one hears a syllable of objection. And every practical man — every man who knows the scene of action — will agree that our system of banking, based on a single reserve in the Bank of England, cannot be altered, or a system of many banks, each keeping its own reserve, be substituted for it; nothing but a revolution would effect it, and there is nothing to cause a revolution.

This being so, there is nothing for it but to make the best of our banking system, and to work it in the best way that it is capable of; we can only use palliatives, and the point is, to get the best palliative we can. I have endeavored to show why it seems to me that the palliatives which I have suggested are the best that are at our disposal.

I have explained why the French plan will not suit our English world. The direct appointment of the Governor and Deputy-Governor of the Bank of England by the executive government would not lessen our evils or help our difficulties; I fear it would rather make both worse. But possibly it may be suggested that I ought to explain why the American system, or some modification, would not or might not be suitable to us. The American law says that each national bank shall have a fixed proportion of cash to its liabilities (there are two classes of banks and two different proportions, but that is not to the present purpose); and it ascertains by inspectors, who inspect at their own times, whether the required amount of cash is in the bank or not. It may be asked, Could nothing like this be attempted in England? could not it, or some modification, help us out of our difficulties? As far as the American banking system is one of many reserves, I have said why I think it is of no use considering whether we should adopt it or not: we cannot adopt it if we would; the one-reserve system is fixed upon us. The only practical imitation of the American system would be, to enact that the Banking Department of the Bank of England should always keep a fixed proportion — say one-third — of its liabilities in reserve; but as we have seen before, a fixed proportion of the liabilities, even when that proportion is voluntarily chosen by the directors and not imposed by law, is not the proper standard for a bank reserve. Liabilities may be imminent or distant, and a fixed rule which imposes the same reserve for both will sometimes err by excess

and sometimes by defect: it will waste profits by over-provision against ordinary danger, and yet it may not always save the Bank, for this provision is often likely enough to be insufficient against rare and unusual dangers. But bad as is this system when voluntarily chosen, it becomes far worse when legally and compulsorily imposed. In a sensitive state of the English money market, the near approach to the legal limit of reserve would be a sure incentive to panic; if one-third were fixed by law, the moment the banks were close to one-third, alarm would begin, and would run like magic. And the fear would be worse because it would not be unfounded, — at least, not wholly: if you say that the Bank shall always hold one-third of its liabilities as a reserve, you say in fact that this one-third shall always be useless, for out of it the Bank cannot make advances, cannot give extra help, cannot do what we have seen the holders of the ultimate reserve ought to do and must do. There is no help for us in the American system: its very essence and principle are faulty.

We must therefore, I think, have recourse to feeble and humble palliatives such as I have suggested. With good sense, good judgment, and good care, I have no doubt that they may be enough; but I have written in vain if I require to say now that the problem is delicate, that the solution is varying and difficult, and that the result is inestimable to us all.

APPENDIX.

NOTE A.

LIABILITIES AND CASH RESERVE OF THE CHIEF BANKING SYSTEMS.

THE following is a comparison of the liabilities to the public, and of the cash reserve, of the banking systems of the United Kingdom, France, Germany, and the United States. For the United Kingdom the figures are the most defective, as they only include the deposits of the Bank of England and of the London joint-stock banks; and the banking reserve of the Bank of England, which is the only cash available against these liabilities, is also the only cash reserve against the similar liabilities of the London private banks, the provincial English banks, and the Scotch and Irish banks. In the case of England, therefore, the method of comparison exhibits a larger proportion of cash to liabilities than what really exists.

(1) ENGLISH BANKING.

Liabilities.	£
Deposits of Bank of England, less estimated joint-stock bank balances, at Dec. 31, 1872, . .	29,000,000
Deposits of London joint-stock banks at Dec. 31, 1872 (see *Economist*, Feb. 8, 1873), . . .	91,000,000
Total liabilities, ...	120,000,000

Reserve of Cash.	£
Banking reserve in Bank of England, . .	13,500,000

Making proportion of cash reserve to liabilities to the public about 11.2 per cent.

(2) BANK OF FRANCE (FEBRUARY, 1873).

Liabilities.	£
Circulation, ...	110,000,000
Deposits, ...	15,000,000
Total liabilities, ...	125,000,000

Reserve of Cash.	£
Coin and bullion in hand, ...	32,000,000

Making proportion of cash reserve to liabilities to the public about 25 per cent.

(3) Banks of Germany (January, 1873).

Liabilities.	£
Circulation, ...	63,000,000
Deposits, ...	8,000,000
Acceptances and indorsements, ...	17,000,000
Total liabilities, ...	88,000,000

Reserve of Cash.	£
Cash in hand, ...	41,000,000

Making proportion of cash reserve to liabilities to the public about 47 per cent.

(4) National Banks of United States (Oct. 3, 1872).

Liabilities.	£
Circulation, ...	67,000,000
Deposits, ...	145,000,000
Total liabilities, ...	212,000,000

Reserve of Cash.	£
Coin and legal tenders in hand, ...	26,000,000

Making proportion of cash reserve to liabilities to the public about 12.3 per cent.

SUMMARY.

	Liabilities to the public.	Cash held.	Proportion of cash to liabilities per cent.
	£	£	
Bank of England and London joint-stock banks, . . .	120,000,000	13,500,000	11.2
Bank of France, ...	125,000,000	32,000,000	25.0
Banks of Germany, ...	88,000,000	41,000,000	47.0
National banks of United States, .	212,000,000	26,000,000	12.3

NOTE B.

EXTRACT FROM EVIDENCE GIVEN BY MR. ALDERMAN SALOMONS BEFORE HOUSE OF COMMONS SELECT COMMITTEE IN 1858.

1146. (CHAIRMAN.) The effect upon yourselves of the pressure in November was, I presume, to induce you to increase your reserve in your own hands, and also to increase your deposits with the Bank of England? — Yes, that was so; but I wish to tell the Committee that that was done almost entirely by allowing the bills of exchange which we held to mature, and not by raising any money or curtailing our accommodation to our customers. Perhaps it may be interesting to the Committee to know that on the 11th of November we held discounted bills for brokers to the amount of £5,623,000; out of those bills £2,800,000 matured between the 11th of November and the 4th of December, and £2,000,000 more between the 4th of December and the 31st: so that about £5,000,000 of bills matured between the 11th of November and the 31st of December; consequently we were prepared, merely by the maturing of our bills of exchange, for any demands that might possibly come upon us.

1147. I understand you to say that you did not withdraw your usual accommodation from your own customers, but that you ceased to have in deposit with the bill-brokers so large a sum of money as you had before? — Not exactly that: the bills which we had discounted were allowed to mature, and we discounted less; we kept a large reserve of cash.

1148. That is to say, you withdrew from the commercial world a part of that accommodation which you had previously given, and at the same time you increased your deposits with the Bank of England? — Yes, our deposits with the Bank of England were increased; we did not otherwise withdraw accommodation.

1149. (Mr. WEGUELIN.) Had you any money at call with the bill-brokers? — A small amount; perhaps about £500,000 or less, which we did not call in.

1150. (CHAIRMAN.) What I understand you to say is, that the effect of the commercial pressure upon you was, to induce you upon the whole to withdraw from commerce an amount of accommodation which in other times you had given, and at the same time to increase your deposits with the Bank of England? — So far only as ceasing to discount with strangers, — persons not having current accounts with us.

1151. Or to give the same amount to the bill-broker? — For a while, instead of discounting for brokers and strangers, we allowed our bills to mature, and remained quiescent with a view to enable us to meet any demand that might be made on ourselves.

1152. Except what you felt bound to your own customers to continue to give, you ceased to make advances? — Quite so; perhaps I might say at the same time that besides a large balance which we kept at the Bank of England, which of course was as available as in our own tills, we increased our notes in our tills at the head office and at all the branches.

1153. I suppose at that time large sales of public securities were made by the London joint-stock banks, which securities were purchased by the public? — It is understood that some joint-stock and other banks sold; but I believe it is quite certain that the public purchased largely, because they always purchase when the funds fall.

1154. Are you prepared to give the Committee any opinion of your own as to the effect, one way or the other, which the system of the joint-stock banks may have produced with regard to aggravating or diminishing the commercial pressure in the autumn of last year? — I should state generally that the joint-stock banks, as well as all other banks, in London, by collecting money from those who had it to spare, must of necessity have assisted and could not do otherwise than assist commerce, both then and at all other times.

1155. You say that your discounts, either at your own counter or through the bill-brokers, are ordinarily very large, but that at the time of severest pressure you contracted them so far as you thought was just to your own immediate customers? — Yes: but the capital was still there, because it was at the Bank of England, and it was capable of being used for short periods; if we did not want it, others might have used it.

1156. (Mr. Weguelin.) In fact, it was used by the Bank of England? — Undoubtedly; I should suppose so; there is no question about it.

1157. You of course felt quite certain that your deposits in the Bank of England might be had upon demand? — We had no doubt about it.

1158. You did not take into consideration the effect of the law of 1844, which might have placed the Banking Department of the Bank of England in such a position as not to be able to meet the demands of its depositors? — I must say that that never gave us the smallest concern.

1159. You therefore considered that if the time should arrive, the government would interfere with some measure, as they had previously done, to enable the Bank to meet the demands upon it? — We should always have thought that if the Bank of England had stopped payment, all the machinery of government would have stopped with it; and we never could have believed that so formidable a calamity would have arisen if the government could have prevented it.

1160. (CHAIRMAN.) The notion of the convertibility of the note being in danger never crossed your mind? — Never for a moment; nothing of the kind.

1161. (Mr. WEGUELIN.) I refer not to the convertibility of the note, but to the state of the Banking Department of the Bank of England. — If we had thought that there was any doubt whatever about it, we should have taken our bank notes and put them in our own strong chest. We could never for a moment believe an event of that kind as likely to happen.

1162. Therefore you think that the measure taken by the government, of issuing a letter authorizing the Bank of England to increase their issues of notes upon securities, was what was generally expected by the commercial world, and what in future the commercial world would look to in such a conjunction of circumstances? — We looked for some measure of that nature; that, no doubt, was the most obvious one. We had great doubts whether it would come when it did, until the very last moment.

1163. Have you ever contemplated the possibility of the Bank refusing to advance, under circumstances similar to those which existed in November, 1857, upon good banking securities? — Of course I have, and it is a very difficult question to answer as to what its effect might be; but the notion appears to me to be so thoroughly ingrained in the minds of the commercial world, that whenever you have good security it ought to be convertible at the Bank in some shape or way, that I have very great doubt indeed whether the Bank can ever take a position to refuse to assist persons who have good commercial securities to offer.

1164. (Mr. CAYLEY.) When you say that you have come to some fresh arrangement with regard to your allowance of interest upon deposits, do you speak of yourselves as the London and Westminster Bank, or of some of the other banks in combination with yourselves? — I think all the banks have come to an understanding that it is not desirable, either for their proprietors or for the public, to follow closely at all times the alterations of the Bank. I believe it is understood amongst them all that they do not intend following that course in future.

1165. Is that from a feeling that it is rather dangerous under particular circumstances? — I cannot admit as to its being dangerous: but there can be no doubt of this, that there is a notion in the public mind which we ought not to contend against, that when you offer a high rate of interest for money, you rather do it because you want the person's money than because you are obeying the market rate; and I think it is desirable that we should show that if persons wish to employ their money, and want an excessive rate, they may take it away and employ it themselves.

1166. You think that there is now a general understanding amongst the banks which you have mentioned, to act upon a different principle from that on which they acted during last October and November? — I think I may say that I know that to be the case.

1167. Was not it the fact that this system of giving so high a rate of interest upon money at call commenced very much with the establishment of some banks during the last year or two, which, instead of demanding ten days' or a month's notice, were willing to allow interest upon only three days' notice; did not that system begin about two years ago? — I do not think it began with the new banks; I think it began with one of the older banks. I know that as regards my own bank, that we were forced into it. I forgot to say that with regard to ourselves in taking money on deposit, the parties must leave the money a month, or they lose interest. We do not take money from any depositor at interest unless upon the understanding and condition that it remains a month with us; he may withdraw it within the month, but then he forfeits interest; it will not carry interest unless it is with us a month, and then it is removable on demand without notice.

1168. Is it or is it not a fact that some of the banks pay interest upon their current accounts? — Yes, I think most of the new banks do so; and the Union Bank of London does it.

1169. At a smaller rate than upon their deposits, I presume? — I think at a smaller rate, but I believe it is a fixed rate on the minimum balance for some period; either six months or one month, I do not exactly know the period. I think I ought to add (and I believe it is the case with all the banks) that the London and Westminster Bank, from the day of its first institution until the present day, has never rediscounted a bill. No bill has ever left our bank unless it has been for payment.

1170. Is not that generally the case with the London joint-stock banks? — I believe it is the case.

1171. (Mr. WEGUELIN.) But you sometimes lend money upon bills deposited with you by bill-brokers? — Yes.

1172. And you occasionally call in that money and redeliver those securities? — Yes; but that we do to a very small extent.

1173. Is not that equivalent to a rediscount of bills? — No; the discount of a bill and the lending money on bills are very different things. When we discount a bill, that bill becomes our property; it is in our control, and we keep it and lock it up until it falls due: but when brokers come to us and want to borrow say £50,000 on a deposit of bills, and we let them have the money, and afterwards return those bills to them and we get back our money, surely that is not a rediscount.

1174. When you want to employ your money for a short period, do you not frequently take bills of long date and advance upon them? — But that is not a rediscount on our part. Very often brokers in borrowing money send in bills of long date, and afterwards we call in that loan; but that is no more a rediscount than lending money upon consols and calling in that money again. It is not an advance of ours, — we do not seek it: they come to us and borrow our money, and give us a security; when we want our money we call for that money, and return their security. Surely that is not a rediscount.

1175. (Mr. HANKEY.) Is there not this clear distinction between returning a bill on which you have made an advance, and discounting a bill, — that if you have discounted a bill, your liability continues upon the bill until that bill has come to maturity? — Yes.

1176. In the other case you have no further liability whatever? — Certainly.

1177. Should you not consider that a very important distinction? — I think it is an important distinction. Take this case: Suppose a party comes to us and borrows £50,000, and we lend it him, and when the loan becomes due we take our money back again, — surely that is not a discount on our part.

1178. Is there not this distinction, — that if you rediscount you may go on pledging the liability of your bank to an almost unlimited amount, whereas in the other case you only get back that money which you have lent? — Undoubtedly.

1179. (Mr. CAYLEY.) The late Chancellor of the Exchequer stated before the adjournment, in a speech in the House of Commons, that during the Monday, Tuesday, Wednesday, and Thursday of the panic, the Bank was almost if not entirely the only body that discounted commercial bills: how can you reconcile that with what you have said, that you gave as much accommodation as usual to your customers? — I am not responsible for what the

Chancellor of the Exchequer said; I am responsible for what I am now stating as to the course of our bank, — that our advances to our customers on the 31st of December were nearly £500,000 higher than they were on the 31st of October. With regard to our not discounting for other parties, it was in consequence of the discredit which prevailed, that it was necessary we should hold a portion of our deposits in order that they should be available in case persons called for them; a certain number of persons did so: in the month of November we had a reduction of our deposits, and if we had gone on discounting for brokers we should have had to go into the market ourselves to raise money on our government securities; but we avoided that by not discounting, and leaving our money at the Bank of England.

1180. Then you did not discount as much as usual for your customers during that period? — Yes, we did, and more.

1181. But not to strangers? — Not to strangers; I make a distinction between our transactions with our customers, who of course expect us to give accommodation, and discounts for brokers, which is entirely voluntary, depending upon our having money to employ.

1182. How would it have been if the letter had not issued at the last moment? — That is a question which I can hardly answer.

1183. What do you mean by that general expression of yours? — It is impossible to predicate what may happen in time of panic and alarm. A great alarm prevailed certainly amongst the commercial world, and it could never have been alleviated except by some extraordinary means of relief; we might probably have been in the state in which Hamburg was, where they have no bank notes in circulation.

1184. (Mr. Spooner.) What did you mean by the expression "the last moment"? You said that the letter came out at the last moment: the last moment of what? — It was late in the day; it was a day of great distress. For two days there was a great deal of anxiety, and everybody expected that there would be some relief: and it was when expectation, I suppose, was highly excited that the letter came, and it gave relief.

1185. Cannot you tell us what your opinion would have been, if that last moment had happened to have elapsed and the letter had not come? — It is very difficult to say; it is too much to say that it could not have been got over. There can be no doubt whatever that what created the difficulty existed out of London, and not in it; and therefore it is much more difficult for me to give an opinion. I believe that the banking interest, both private

and joint-stock, was in a perfectly sound condition, and able to bear any strain which might have been brought upon it in London.

1186. (Mr. HANKEY.) Can you give the Committee any idea as to what proportion of deposits you consider generally desirable to keep in reserve? — You must be very much guided by circumstances. In times of alarm, when there are failures, of course all bankers strengthen their reserves; our reserve then is larger. In times of ordinary business we find, both as regards our deposits at interest as well as those which are not at interest, that there is a constant circulation; that the receipts of money very nearly meet the payments.

1187. You probably keep at all times a certain amount of your deposits totally unemployed, — in reserve? — Yes.

1188. In a normal state of commercial affairs, is there any fixed proportion, or can you give the Committee any idea of what you would consider about a fair and desirable proportion, which should be so kept unemployed? — I think the best idea which I can give upon that subject is to give our annual statement, or balance sheet for the 31st of December.

1189. Does that show what amount of unemployed money you had on that day? — Yes. I will put in a statement, which perhaps will be the best means of meeting the question, showing the cash in hand on the 30th of June and the 31st of December in every year, as shown by our published accounts, together with our money at call and our government securities; that will be perhaps the best and most convenient way of giving the information you desire to have. [*See Table on next page.*]

1190. Do you consider that when your deposits are materially on the increase, it is necessary to keep a larger amount of money in reserve than you would keep at other times? — I may say that as a general rule, our reserve would always bear some proportion to our deposits.

1191. Do you employ your money in the discounting of bills for other persons than your own customers? — Discount brokers.

1192. Only to discount brokers? — Yes.

1193. Not to strangers who are in the habit of bringing you in bills, — commercial houses? — I should say generally not. We have one or two houses for whom we discount who have not accounts with us as bankers; but generally we do not discount except for our customers or for bill-brokers.

1194. Do you consider that any advantage can arise to the public by the Bank of England advancing to a greater extent than can be considered strictly prudent on the soundest principle

Total Lodgments with London and Westminster Bank; also Amount of Cash in Hand, Moneys with Bill-Brokers at Call, and Government Securities held by the Bank.

DATE.	Deposits.	Cash in Hand.	Money at Call.	Government Securities.	Total.
	£	£.	£.	£.	£.
31 December, 1845,	3,590,014	563,072	628,500	1,039,745	2,231,317
" " 1846,	3,280,864	634,575	423,060	938,717	1,996,352
" " 1847,	2,733,753	721,325	350,108	791,899	1,863,332
30 June, 1848,	3,170,118	588,871	159,724	1,295,047	2,043,642
31 December, "	3,089,659	645,468	176,824	1,189,213	2,011,505
30 June, 1849,	3,392,857	552,642	246,494	964,800	1,763,936
31 December, "	3,680,623	686,761	263,577	973,691	1,224,029
30 June, 1850,	3,821,022	654,649	258,177	972,055	1,884,881
31 December, "	3,969,648	566,039	334,982	1,089,794	1,990,815
30 June, 1851,	4,414,179	691,719	424,195	1,054,018	2,169,932
31 December, "	4,677,298	653,946	378,337	1,054,018	2,080,301
30 June, 1852,	5,245,135	861,778	206,687	1,054,018	2,122,483
31 December, "	5,581,706	855,057	397,087	1,119,477	2,371,621
30 June, 1853,	6,219,817	904,252	499,467	1,218,852	2,622,571
31 December, "	6,259,540	791,699	677,392	1,468,902	2,937,993
30 June, 1854,	6,892,470	827,397	917,557	1,457,415	3,202,369
31 December, "	7,177,244	694,309	486,400	1,451,074	2,631,783
30 June, 1855,	8,166,553	722,243	483,890	1,754,074	2,960,207
31 December, "	8,744,095	847,856	451,575	1,949,074	3,248,505
30 June, 1856,	11,170,010	906,876	601,800	1,980,489	3,489,165
31 December, "	11,438,461	1,119,591	432,000	2,922,625	4,474,216
30 June, 1857,	13,913,058	967,078	687,730	3,353,179	5,007,987
31 December, "	13,889,021	2,226,441	1,115,883	3,582,797	6,925,121

of banking, under the idea of their affording aid to the commercial world? — As I said before, as long as there are good bills in circulation, — that is, bills about which there would be no doubt of their being paid at maturity, — there should be some means by which those bills could be discounted.

1195. And do you think that it is part of the functions of the Bank of England to discount a bill for anybody, merely because the party holding the bill wishes to convert it into cash? — As I said before, the Bank of England will have great difficulty in getting rid of that inconvenient idea which there is in the mind of the public, that the Bank of England is something more than an ordinary joint-stock bank. I think it must depend very much upon circumstances whether you can or cannot refuse the discount of good bills which are offered to you.

NOTE C.

STATEMENT OF CIRCULATION AND DEPOSITS OF THE BANK OF DUNDEE AT INTERVALS OF TEN YEARS BETWEEN 1764 AND 1864.

Year.	Circulation.	Deposits.*
	£.	£.
1764,	30.395	—
1774,	27,670	—
1784,	56,342	—
1794,	50,254	48,809
1804,	54,096	157,821
1814,	46,627	445,066
1824,	29,675	343,948
1834,	26,467	563,202
1844,	27,504	535,253
1854,	40,774	705,222
1864,	41,118	684,898

* The bank did not begin to receive deposits until 1792, in which year they amounted to £35,944.

NOTE D.

MEETING OF THE PROPRIETORS OF THE BANK OF ENGLAND,

Sept. 13, 1866.

(*From "Economist," Sept.* 22, 1866.)

A General Court of the Bank of England was held at the Bank at twelve o'clock on the 13th instant, for the purpose of declaring a dividend for the past half-year.

Mr. Launcelot Holland, the Governor of the Bank, who presided upon the occasion, addressed the proprietors as follows: —

"This is one of the quarterly general courts appointed by our charter; and it is also one of our half-yearly general courts, held under our by-laws, for the purpose of declaring a dividend. From a statement which I hold in my hand, it appears that the net profits of the Bank for the half-year ending on the 31st of August last amounted to £970,014 17*s.* 10*d.*, making the amount of the rest on that day £3,981,783 18*s.* 11*d.*; and after providing for a dividend at the rate of £6 10*s.* per cent., the rest will stand at £3,035,838 18*s.* 11*d.* The Court of Directors, therefore, propose

that a half-yearly dividend of interest and profits, to the amount of £6 10*s.* per cent., without deduction on account of income tax, shall be made on the 10th of October next. That is the proposal I have now to lay before the general court; but as important events have occurred since we last met, I think it right I should briefly advert to them upon this occasion. A great strain has within the last few months been put upon the resources of this house, and of the whole banking community of London; and I think I am entitled to say that not only this house, but the entire banking body, acquitted themselves most honorably and creditably throughout that very trying period. Banking is a very peculiar business, and it depends so much upon credit that the least blast of suspicion is sufficient to sweep away, as it were, the harvest of a whole year; but the manner in which the banking establishments generally of London met the demands made upon them during the greater portion of the past half-year affords a most satisfactory proof of the soundness of the principles on which their business is conducted. This house exerted itself to the utmost — and exerted itself most successfully — to meet the crisis; we did not flinch from our post. When the storm came upon us, on the morning on which it became known that the house of Overend & Co. had failed, we were in as sound and healthy a position as any banking establishment could hold, and on that day and throughout the succeeding week we made advances which would hardly be credited; I do not believe that any one would have thought of predicting, even at the shortest period beforehand, the greatness of those advances. It was not unnatural that in this state of things a certain degree of alarm should have taken possession of the public mind, and that those who required accommodation from the Bank should have gone to the Chancellor of the Exchequer and requested the government to empower us to issue notes beyond the statutory amount, if we should think that such a measure was desirable. But we had to act before we could receive any such power, and before the Chancellor of the Exchequer was perhaps out of his bed we had advanced one-half of our reserves, which were certainly thus reduced to an amount which we could not witness without regret: but we could not flinch from the duty which we conceived was imposed upon us of supporting the banking community, and I am not aware that any legitimate application for assistance made to this house was refused. Every gentleman who came here with adequate security was liberally dealt with; and if accommodation could not be afforded to the full extent which was demanded, no one who offered proper security failed

to obtain relief from this house. I have perhaps gone a little more into details than is customary upon these occasions; but the times have been unusually interesting, and I thought it desirable to say this much in justification of the course adopted by this house, of running its balances down to a point which some gentlemen may consider dangerous. Looking back, however, upon recent events, I cannot take any blame to this court for not having been prepared for such a tornado as that which burst upon us on the 11th of May; and I hope the Court of Proprietors will feel that their directors acted properly upon that occasion, and that they did their best to meet a very extraordinary state of circumstances. I have now only to move that a dividend be declared at the rate of £6 10*s.* per cent. for the past half-year."

Mr. Hyam said that before the question was put, he wished to offer a few observations to the court. He believed that the statement of accounts which had just been laid before them was perfectly satisfactory. He also thought that the directors had done their best to assist the commercial classes throughout the late monetary crisis; but it appeared to him at the same time that they were in fault in not having applied at an earlier period to the Chancellor of the Exchequer for a suspension of the Bank Act. It was well known that the demand on the Bank was materially lessened in the earlier part of the day, in consequence of a rumor which had been extensively circulated that permission to overstep the limits laid down in the Act had been granted. That concession, however, had only been made after the most urgent representations had been addressed to the Chancellor of the Exchequer at a late hour in the night; and if it had then been refused, he felt persuaded that the state of affairs would have been much worse on the Saturday than it had been on the Friday. The fact was, that the Act of 1844 was totally unsuited to the present requirements of the country, which since that period had tripled or quadrupled its commerce; and he was sorry to know that the measure seemed to meet with the approval of many of their directors. Any one who read the speeches made in the course of the discussion on Mr. Watkins's motion must see that the subject called for further inquiry; and he trusted that the demand for that inquiry would yet be conceded.

Mr. Jones said he entirely dissented from the views with respect to the Bank Act entertained by the honorable proprietor who had just addressed the court. In his opinion the main cause of the recent monetary crisis was, that while we had bought £275,000,000 worth of foreign produce in the year 1865, the value of our exports

had only been £165,000,000, so that we had a balance against us to the amount of £110,000,000. He believed that the Bank acted wisely in resisting every attempt to increase the paper currency, and he felt convinced that the working classes would be the people least likely to benefit by the rise in prices which would take place under such a change.

Mr. Moxon said he should be glad to know what was the amount of bad debts made by the Bank during the past half-year. It was stated very confidently out of doors that during that period the directors had between £3,000,000 and £4,000,000 of bills returned to them.

The Governor of the Bank.— "May I ask what is your authority for that statement? We are rather amused at hearing it, and we have never been able to trace any rumor of the kind to an authentic source."

Mr. Moxon continued.—Whether the bad debts were large or small, he thought it was desirable that they should all know what was their actual amount. They had been told at their last meeting that the Bank held a great many railway debentures; and he should like to know whether any of those debentures came from railway companies that had since been unable to meet their obligations. He understood that a portion of their property was locked up in advances made on account of the Thames Embankment, and in other ways which did not leave the money available for general banking and commercial purposes; and if that were so, he should express his disapproval of such a policy. There was another important point to which he wished to advert: he was anxious to know what was the aggregate balance of the joint-stock banks in the Bank of England. He feared that some time or other the joint-stock banks would be in a position to command perhaps the stoppage of the Bank of England. If that were not so, the sooner the public were fully informed upon the point the better; but if ten or twelve joint-stock banks had large balances in the Bank of England, and if the Bank balances were to run very low, people would naturally begin to suspect that the joint-stock banks had more power over the Bank of England than they ought to have. He wished further to ask whether the directors had of late taken into consideration the expediency of paying interest on deposits. He believed that under their present mode of carrying on their business, they were foregoing large profits which they might receive with advantage to themselves and to the public; and he would recommend that they should undertake the custody of securities, after the system adopted by the Bank of France. In conclusion, he

proposed to move three resolutions, for the purpose of providing, first, that a list of all the proprietors of Bank stock should be printed, with a separate entry of the names of all those persons not entitled to vote from the smallness of their stock or from the shortness of time during which they held it; secondly, that a copy of the charter of the Bank, with the rules, orders, and by-laws passed for the good government of their corporation, should be printed for the use of the shareholders; and thirdly, that auditors should be appointed to make detailed audits of their accounts.

Mr. Gerstenberg recommended that the directors should take some step for the purpose of preventing the spread of such erroneous notions as that which lately prevailed on the Continent, that the Bank was about to suspend specie payments.

Mr. W. Botly said he wished to see the directors taking into their consideration the expediency of allowing interest on deposits.

Mr. Alderman Salomons said he wished to take that opportunity of stating that he believed nothing could be more satisfactory to the managers and shareholders of joint-stock banks than the testimony which the Governor of the Bank of England had that day borne to the sound and honorable manner in which their business was conducted. It was manifestly desirable that the joint-stock banks and the banking interest generally should work in harmony with the Bank of England; and he sincerely thanked the Governor of the Bank for the kindly manner in which he had alluded to the mode in which the joint-stock banks had met the late monetary crisis.

The Governor of the Bank said — "Before putting the question for the declaration of a dividend, I wish to refer to one or two points that have been raised by the gentlemen who have addressed the Court on this occasion. The most prominent topic brought under our notice is the expediency of allowing interest on deposits; and upon that point, I must say that I believe a more dangerous innovation could not be made in the practice of the Bank of England. The downfall of Overend & Gurney, and of many other houses, must be traced to the policy which they adopted of paying interest on deposits at call, while they were themselves tempted to invest the money so received in speculations in Ireland or in America, or at the bottom of the sea, where it was not available when a moment of pressure arrived."

Mr. Botly said he did not mean deposits on call.

The Governor of the Bank of England continued — "That is only a matter of detail: the main question is, whether we ought to pay interest on deposits; and of such policy I must express my

entire disapproval. Mr. Moxon has referred to the amount of our debts; but as I stated when I took the liberty of interrupting him, we could never trace the origin of any rumor which prevailed upon that subject. As far as it can be said to have ever existed, it had its origin most probably in the vast amount advanced by the Bank. It must, however, be remembered that we did not make our advances without ample security; and the best proof of that is the marvelously small amount of bad debts which we contracted. It has never been a feature of the Bank to state what was the precise amount of those debts; but I believe that if I were to mention it upon the present occasion, it would be found to be so inconsiderable that I should hardly obtain credence for the announcement I should have to make. I am convinced that our present dividend has been as honestly and as hardly earned as any that we have ever realized; but it has been obtained by means of great vigilance and great anxiety on the part of each and all of your directors; and I will add that I believe you would only diminish their sense of responsibility, and introduce confusion into the management of your business, if you were to transfer to auditors the making up of your accounts. If your directors deserve your confidence, they are surely capable of performing that duty; and if they do not deserve it, you ought not to continue them in their present office. With regard to the supposed lock-up of our capital, I must observe that with £14,000,000 on our hands, we must necessarily invest it in a variety of securities; but there is no ground for imagining that our money is locked up and is not available for the purpose of making commercial advances. We advanced in the space of three months the sum of £45,000,000; and what more than that do you want? It has been recommended that we should take charge of securities; but we have found it necessary to refuse all securities except those of our customers, and I believe the custody of securities is becoming a growing evil. With regard to railway debentures, I do not believe we have one of a doubtful character; we have no debentures except those of first-class railway companies, and companies which we know are acting within their parliamentary limits. Having alluded to those subjects, I will now put the motion for the declaration of the dividend."

The motion was accordingly put and unanimously adopted.

The chairman then announced that that resolution should be confirmed by ballot on Tuesday next; inasmuch as the Bank could not, under the provisions of its Act of Parliament, declare otherwise than in that form a dividend higher than that which it had distributed during the preceding half-year.

The three resolutions proposed by Mr. Moxon were then read; but they were not put to the meeting, inasmuch as they found no seconders.

Mr. Alderman Salomons said that their Governor had observed that he thought the payment of interests on deposits was objectionable; and every one must see that such a practice ought not to be adopted by the Bank of England. But he took it for granted that the Governor did not mean that his statement should apply to joint-stock banks, which he had himself told them had conducted their business so creditably and so successfully.

The Governor of the Bank said that what he stated was, that such a system would be dangerous for the Bank of England, and dangerous if carried into effect in the way contemplated by Mr. Moxon.

Mr. P. N. Laurie said he understood the Governor of the Bank to say that it would be dangerous to take deposits on call, and in that opinion he concurred.

Mr. Alderman Salomons said that he too was of the same opinion.

On the motion of Mr. Alderman Salomons, seconded by Mr. Botly, a vote of thanks was passed to the Governor and the directors for their able and successful management of the Bank during the past half-year; and the proceedings then terminated.

ECONOMIC STUDIES.

PREFATORY NOTE.

It will be obvious to the readers of this book that a considerable portion of it, though hardly to be called fragmentary, is yet not at all as complete as the author, had he lived, would have made it; and that, in the last two essays at all events, there are considerable gaps which he would certainly have filled up. Obviously, too, various other essays would have been added; probably two or three between those which here appear, certainly many on subjects which would naturally have followed the last and least perfect of all the papers, that on "Cost of Production." Indeed, Mr. Bagehot is known to have stated that his economic studies would have worked out into three distinct volumes, one of which would have been biographical. Again, no careful reader can fail to perceive that there is a certain amount of redundancy of statement in these pages, as well as of omission; and this was inevitable, for in preparing his finished writings for the press, the author's practice was to cut away as well as to add much, — a duty which I was not imprudent enough to attempt to discharge for him. Therefore, considering that only the first two essays had been published, or even printed, in the lifetime of the author, and that, even with the most valuable help of Mr. Robert Giffen, the head of the

Statistical Department of the Board of Trade (who, during the last years of Mr. Bagehot's life, had a better knowledge of his economic mind than any other person), I have had great difficulty in determining the precise arrangement of some parts of the MS., the folios of which were often inaccurately numbered, I hope that the reader may wonder less that much is incomplete than that so much that is complete and valuable, as well as original, remains. No thoughtful economist, I am sure, who reads this book, will fail to recognize the value of a great portion of even the least perfect of these essays.

It only remains for me to express my hearty gratitude to Mr. Giffen for his willing and most important help, without which I should have felt no little hesitation in deciding on the true sequence of some passages in this volume. R. H. H.

August 30, 1879.

THE POSTULATES

OF

ENGLISH POLITICAL ECONOMY.

ADAM SMITH completed the "Wealth of Nations" in 1776, and our English political economy is therefore just a hundred years old. In that time it has had a wonderful effect: the life of almost every one in England — perhaps of every one — is different and better in consequence of it; the whole commercial policy of the country is not so much founded on it as instinct with it; ideas which are paradoxes everywhere else in the world are accepted axioms here as results of it. No other form of political philosophy has ever had one-thousandth part of the influence on us; its teachings have settled down into the common-sense of the nation, and have become irreversible.

We are too familiar with the good we have thus acquired to appreciate it properly; to do so we should see what our ancestors were taught. The best book on political economy published in England before that of Adam Smith is Sir James Steuart's "Inquiry," a book full of acuteness, and written by a man of travel and cultivation; and its teaching is of this sort: —

"In all trade two things are to be considered in the commodity sold; the first is the matter, the second is the labor employed to render this matter useful. The matter exported from a country is what the country loses; the price of the labor exported is what it gains. If the value of the matter imported be greater than the value of what is exported, the country gains; if a greater value of labor be imported than exported, the country loses. Why? Because in the first case strangers must have paid *in matter* the

surplus of labor exported; and in the second case because the country must have paid to strangers *in matter* the surplus of labor imported. It is therefore a general maxim to discourage the importation of work, and to encourage the exportation of it."*

It was in a world where *this* was believed that our present political economy began.

Abroad the influence of our English system has of course not been nearly so great as in England itself; but even there it has had an enormous effect, — all the highest financial and commercial legislation of the Continent has been founded upon it. As curious a testimony perhaps as any to its power is to be found in the memoir of Mollien, the financial adviser of the first Napoleon; *le bon Mollien*, whom nothing would induce him to discard because his administration brought *francs*, whereas that of his more showy competitors might after all end in *ideas*.

"It was then," says Mollien, in giving an account of his youth, "that I read an English book of which the disciples whom M. Turgot had left spoke with the greatest praise, — the work of Adam Smith. I had especially remarked how warmly the venerable and judicious Malesherbes used to speak of it, — this book so deprecated by all the men of the old routine, who spoke of themselves so improperly as of the school of Colbert. They seemed to have persuaded themselves that the most important thing for our nation was, that not one *sou* should ever leave France; that so long as this was so, the kind and the amount of taxation, the rate of wages, the greater or less perfection of industrial arts, were things of complete indifference, provided always that one Frenchman gained what another Frenchman lost." †

And he describes how the "Wealth of Nations" led him to abandon those absurdities and to substitute the views with which we are now so familiar, but on which "the good Mollien" dwells as on new paradoxes. In cases like this, one instance is worth a hundred arguments: we see in a moment the sort

* Book ii., Chap. xxiv.

† See also M. Chevalier's article on Mollien, *Revue des Deux Mondes*, July-August, 1856. — Ed.

of effect that our English political economy has had when we find it guiding the finance of Napoleon, who hated ideologues and who did not love the English.

But notwithstanding these triumphs, the position of our political economy is not altogether satisfactory: it lies rather dead in the public mind; not only does it not excite the same interest as formerly, but there is not exactly the same confidence in it. Younger men either do not study it, or do not feel that it comes home to them, and that it matches with their most living ideas; new sciences have come up in the last few years, with new modes of investigation, and they want to know what is the relation of economical science as their fathers held it to these new thoughts and these new instruments. They ask, often hardly knowing it, "Will this 'science,' as it claims to be, harmonize with what we now know to be sciences, or bear to be tried as we now try sciences?" and they are not sure of the answer.

Abroad, as is natural, the revolt is more avowed. Indeed, though the political economy of Adam Smith penetrated deep into the Continent, what has been added in England since has never penetrated equally; though if our "science" is true, the newer work required a greater intellectual effort, and is far more complete as a scientific achievement, than anything which Adam Smith did himself. Political economy as it was taught by Ricardo has had in this respect much the same fate as another branch of English thought of the same age, with which it has many analogies, — jurisprudence as it was taught by Austin and Bentham: it has remained insular. I do not mean that it was not often read and understood, — of course it was so, though it was often misread and misunderstood; but it never at all reigned abroad as it reigns here, — never was really fully accepted in other countries as it was here where it arose. And no theory, economical or political, can now be both insular and secure: foreign thoughts come soon

and trouble us; there will always be doubt here as to what is only believed here.

There are, no doubt, obvious reasons why English political economy should be thus unpopular out of England: it is known everywhere as the theory "of Free Trade," and out of England Free Trade is almost everywhere unpopular. Experience shows that no belief is so difficult to create and no one so easy to disturb; the Protectionist creed rises like a weed in every soil. "Why," M. Thiers was asked, "do you give these bounties to the French sugar refiners?" "I wish," replied he, "the tall chimneys to smoke." Every nation wishes prosperity for some conspicuous industry; at what cost to the consumer, by what hardship to less conspicuous industries, that prosperity is obtained, it does not care. Indeed, it hardly knows, it will never read, it will never apprehend the refined reasons which prove those evils and show how great they are: the visible picture of the smoking chimneys absorbs the whole mind. And in many cases the eagerness of England in the Free Trade cause only does that cause harm. Foreigners say, "Your English traders are strong and rich: of course you wish to undersell our traders, who are weak and poor. You have invented this political economy to enrich yourselves and ruin us: we will see that you shall not do so."

And that English political economy is more opposed to the action of government in all ways than most such theories brings it no accession of popularity. All governments like to interfere,—it elevates their position to make out that they can cure the evils of mankind: and all zealots wish they should interfere, for such zealots think they can and may convert the rulers and manipulate the state control,—it is a distinct object to convert a definite man, and if he will not be convinced there is always a hope of his successor; but most zealots dislike to appeal to the mass of mankind,—they know instinctively

that it will be too opaque and impenetrable for them.

But I do not believe that these are the only reasons why our English political economy is not estimated at its value abroad. I believe that this arises from its special characteristic, from that which constitutes its peculiar value; and paradoxical as it may seem, I also believe that this same characteristic is likewise the reason why it is often not thoroughly understood in England itself. The science of political economy, as we have it in England, may be defined as the science of business, such as business is in large productive and trading communities; it is an analysis of that world so familiar to many Englishmen, — the "great commerce" by which England has become rich. It assumes the principal facts which make that commerce possible, and as is the way of an abstract science, it isolates and simplifies them; it detaches them from the confusion with which they are mixed in fact. And it deals too with the men who carry on that commerce and who make it possible. It assumes a sort of human nature such as we see everywhere around us, and again it simplifies that human nature; it looks at one part of it only. Dealing with matters of "business," it assumes that man is actuated only by motives of business: it assumes that every man who makes anything makes it for money, that he always makes that which brings him in most at least cost, and that he will make it in the way that will produce most and spend least; it assumes that every man who buys, buys with his whole heart, and that he who sells, sells with his whole heart, each wanting to gain all possible advantage. Of course we know that this is not so, that men are not like this, but we assume it for simplicity's sake as a hypothesis; and this deceives many excellent people, for from deficient education they have very indistinct ideas what an abstract science is.

More competent persons, indeed, have understood that English political economists are not speaking of real men but of imaginary ones, not of men as we see them but of men as it is convenient to us to suppose they are; but even they often do not understand that the world which our political economists treat of is a very limited and peculiar world also. They often imagine that what they read is applicable to all states of society, and to all equally; whereas it is only true of — and only proved as to — states of society in which commerce has largely developed, and where it has taken the form of development, or something near the form, which it has taken in England.

This explains why abroad the science has not been well understood: commerce as we have it in England is not so full-grown anywhere else as it is here, — at any rate, is not so outside the lands populated by the Anglo-Saxon race. Here it is not only a thing definite and observable, but about the most definite thing we have, the thing which it is most difficult to help seeing; but on the Continent, though there is much that is like it, and though that much is daily growing more, there is nowhere the same pervading entity, — the same patent, pressing, and unmistakable object.

And this brings out too the inherent difficulty of the subject; a difficulty which no other science, I think, presents in equal magnitude. Years ago I heard Mr. Cobden say at a League meeting that "Political economy was the highest study of the human mind, for that the physical sciences required by no means so hard an effort." An orator cannot be expected to be exactly precise, and of course political economy is in no sense the highest study of the mind, — there are others which are much higher, for they are concerned with things much nobler than wealth or money; nor is it true that the effort of mind which political economy requires is nearly

as great as that required for the abstruser theories of physical science, — for the theory of gravitation or the theory of natural selection: but nevertheless what Mr. Cobden meant, had — as was usual with his first-hand mind — a great fund of truth. He meant that political economy — effectual political economy, political economy which in complex problems succeeds — is a very difficult thing; something altogether more abstruse and difficult, as well as more conclusive, than that which many of those who rush in upon it have a notion of. It is an abstract science which labors under a special hardship: those who are conversant with its abstractions are usually without a true contact with its facts; those who are in contact with its facts have usually little sympathy with and little cognizance of its abstractions. Literary men who write about it are constantly using what a great teacher calls "unreal words," — that is, they are using expressions with which they have no complete vivid picture to correspond. They are like physiologists who have never dissected, like astronomers who have never seen the stars; and in consequence, just when they seem to be reasoning at their best their knowledge of the facts falls short. Their primitive picture fails them, and their deduction altogether misses the mark; sometimes indeed goes astray so far that those who live and move among the facts, boldly say that they cannot comprehend "how any one can talk such nonsense." Yet on the other hand, these people who live and move among the facts, often or mostly cannot of themselves put together any precise reasonings about them. Men of business have a solid judgment, a wonderful guessing power of what is going to happen, each in his own trade, but they have never practiced themselves in reasoning out their judgments and in supporting their guesses by argument; probably if they did so, some of the finer and correcter parts of their anticipations would vanish. They

are like the sensible lady to whom Coleridge said, "Madam, I accept your conclusion, but you must let me find the logic for it." Men of business can no more put into words much of what guides their life than they could tell another person how to speak their language. And so the "theory of business" leads a life of obstruction, because theorists do not see the business and the men of business will not reason out the theories: far from wondering that such a science is not completely perfect, we should rather wonder that it exists at all.

Something has been done to lessen the difficulty by statistics; these give tables of facts which help theoretical writers and keep them straight: but the cure is not complete. Writers without experience of trade are always fancying that these tables mean something more than, or something different from, that which they really mean. A table of prices, for example, seems an easy and simple thing to understand, and a whole literature of statistics assumes that simplicity; but in fact there are many difficulties. At the outset there is a difference between the men of theory and the men of practice. Theorists take a table of prices as facts settled by unalterable laws: a stock-broker will tell you such prices can be "made,"—in actual business such is his constant expression; if you ask him what is the price of such a stock, he will say, if it be a stock at all out of the common, "I do not know, sir: I will go on to the market and get them to *make* me a price." And the following passage from the Report of the late Foreign Loans Committee shows what sort of process "making" a price sometimes is:—

"Immediately," they say, "after the publication of the prospectus,"—the case is that of the Honduras Loan,—"and before any allotment was made, M. Lefevre authorized extensive purchases and sales of loans on his behalf; brokers were employed by him to deal in the manner best calculated to maintain the price of the stock; the brokers so employed, instructed jobbers to purchase

the stock when the market required to be strengthened, and to sell it if the market was sufficiently firm. In consequence of the market thus created, dealings were carried on to a very large amount: fifty or a hundred men were in the market dealing with each other and the brokers all round; one jobber had sold the loan (£2,500,000) once over."

Much money was thus abstracted from credulous rural investors; and I regret to say that book statists are often equally, though less hurtfully, deceived. They make tables in which artificial prices run side by side with natural ones; in which the price of an article like Honduras scrip, which can be indefinitely manipulated, is treated just like the price of consols, which can scarcely be manipulated at all. In most cases it never occurs to the maker of the table that there could be such a thing as an artificial — a *mala fide* — price at all; he imagines all prices to be equally straightforward. Perhaps, however, this may be said to be an unfair sample of price difficulties, because it is drawn from the Stock Exchange, the most complex market for prices: and no doubt the Stock Exchange has its peculiar difficulties, of which I certainly shall not speak lightly; but on the other hand, in one cardinal respect it is the simplest of markets, — there is no question in it of the physical quality of commodities. One Turkish bond of 1858 is as good or bad as another, one ordinary share in a railway exactly the same as any other ordinary share; but in other markets each sample differs in quality, and it is a learning in each market to judge of qualities, so many are they and so fine their gradations. Yet mere tables do not tell this, and cannot tell it. Accordingly, in a hundred cases you may see "prices" compared as if they were prices of the same thing, when in fact they are prices of different things. The *Gazette* average of corn is thus compared incessantly, yet it is hardly the price of the same exact quality of corn in any two years; it is an average of all the prices in all the sales in all

the markets. But this year the kind of corn mostly sold may be very superior, and last year very inferior; yet the tables compare the two without noticing the difficulty. And when the range of prices runs over many years, the figures are even more treacherous, for the names remain while the quality — the thing signified — is changed; and of this, persons not engaged in business have no warning. Statistical tables, even those which are most elaborate and careful, are not substitutes for an actual cognizance of the facts; they do not, as a rule, convey a just idea of the movements of a trade to persons not *in* the trade.

It will be asked, Why do you frame such a science, if from its nature it is so difficult to frame it? The answer is, that it is necessary to frame it, or we must go without important knowledge. The facts of commerce, especially of the great commerce, are very complex; some of the most important are not on the surface, some of those most likely to confuse *are* on the surface: if you attempt to solve such problems without some apparatus of method, you are as sure to fail as if you try to take a modern military fortress — a Metz or a Belfort — by common assault; you must have guns to attack the one, and method to attack the other.

The way to be sure of this is, to take a few new problems, such as are forever presented by investigation and life, and to see what by mere common-sense we can make of them. For example, it is said that the general productiveness of the earth is less or more in certain regular cycles, corresponding with perceived changes in the state of the sun: what would be the effect of this cyclical variation in the efficiency of industry upon commerce? Some hold — and as I think, hold justly — that, extraordinary as it may seem, these regular changes in the sun have much to do with the regular recurrence of difficult times in the money market. What common-sense would be able to answer these questions? Yet we

may be sure that if there be a periodical series of changes in the yielding power of this planet, that series will have many consequences on the industry of men, whether those which have been suggested or others.

Or to take an easier case, who can tell without instruction what is likely to be the effect of the new loans of England to foreign nations? We press upon half-finished and half-civilized communities incalculable sums; we are to them what the London money-dealers are to students at Oxford and Cambridge. We enable these communities to read in every newspaper that they can have ready money, almost of any amount, on "personal security." No incipient and no arrested civilizations ever had this facility before; what will be the effect on such civilizations now, no untutored mind can say.

Or again: Since the Franco-German war an immense sum of new money has come to England; England has become the settling-place of international bargains much more than it was before: but whose mind could divine the effect of such a change as this, except it had a professed science to help it?

There are indeed two suggested modes of investigation, besides our English political economy and competing with it. One is the Enumerative—or if I may coin such a word, the "All-Case"—method. One school of theorists say—or assume oftener than they say—that you should have a "complete experience"; that you should accumulate all the facts of these subjects before you begin to reason. A very able German writer has said in the *Fortnightly Review*,* of a great economical topic, banking:—

"I venture to suggest that there is but one way of arriving at such knowledge and truth;"—that is, absolute truth and full knowledge—"namely, a thorough investigation of the facts of the case. By 'the facts,' I mean not merely such facts as present themselves to so-called practical men in the common routine of

* September, 1873. Gustav Cohn, "History and Present State of Political Economy in Germany."

business, but the facts which a complete historical and statistical inquiry would develop. When such a work shall have been accomplished, German economists may boast of having mastered the principles of banking; that is to say, of German banking, but not even then of banking in general. To set forth principles of banking in general, it will be necessary to master in the same way the facts of English, Scotch, French, and American banking, — of banking, in short, in every country where banking exists." "The only," he afterwards continues, "but let us add also, the safe ground of hope for political economy is, following Bacon's exhortation, to recommence afresh the whole work of economic inquiry.* In what condition would chemistry, physics, geology, zoölogy be, and the other branches of natural science which have yielded such prodigious results, if their students had been content to spin chains of deduction from the assumptions and speculations of the last century?"

But the reply is, that the method which Mr. Cohn suggests was tried in physical science and failed. And it is very remarkable that he should not have remembered it as he speaks of Lord Bacon; for the method which he suggests is exactly that which Lord Bacon himself followed, and owing to the mistaken nature of which he discovered nothing. The investigation into the nature of heat in the "Novum Organum" is exactly such a collection of facts as Mr. Cohn suggests; but nothing comes of it. As Mr. Jevons well says, Lord Bacon's "notion of scientific method was that of a kind of scientific book-keeping: facts were to be indiscriminately gathered from every source, and posted in a kind of ledger, from which would emerge in time a clear balance of truth. It is difficult to imagine a less likely way of arriving at great discoveries."† And yet it is precisely that from which, mentioning Bacon's name but not forewarned by his experience, Mr. Cohn hopes to make them.

The real plan that has answered in physical science is much simpler. The discovery of a law of

*"There remains the sole safety and health, that the entire work be recommenced as a whole." — Preface to the "Novum Organum."

†"Principles of Science," Vol. ii., page 220. *Cf.* De Morgan's "Budget of Paradoxes," page 56: — "What are large collections of facts for? To make theories *from*, says Bacon; to try ready-made theories *by*, says the history of discovery: it's all the same, says the idolater; nonsense, say we!"

nature is very like the discovery of a murder: in the one case you arrest a suspected person, and in the other you isolate a suspected cause. When Newton, by the fall of the apple or something else, was led to think that the attraction of gravitation would account for the planetary motions, he took that cause by itself, traced out its effects by abstract mathematics, and so to say, found it "guilty,"—he discovered that it would produce the phenomenon under investigation. In the same way geology has been revolutionized in our own time by Sir Charles Lyell: he for the first time considered the effects of one particular set of causes by themselves; he showed how large a body of facts could be explained on the hypothesis "that the forces now operating upon and beneath the earth's surface" are "the same both in kind and degree as those which, at remote epochs, have worked out geological changes."* He did not wait to begin his inquiry till his data about all kinds of strata, or even about any particular kind, were complete: he took palpable causes as he knew them, and showed how many facts they would explain; he spent a long and most important life in fitting new facts into an abstract and youthful speculation. Just so in an instance which has made a literature and gone the round of the world: Mr. Darwin, who is a disciple of Lyell, has shown how one *vera causa*, "natural selection," would account for an immense number of the facts of nature,—for how many, no doubt, is controverted, but as is admitted, for a very large number; and this he showed by very difficult pieces of reasoning, which very few persons would have thought of, and which most people found at first not at all easy to comprehend. The process by which physical science has become what it is, has not been that of discarding abstract speculations, but of working out abstract speculations. The most important known laws of nature, the laws of motion,—the

*Preface to Tenth Edition of "Principles of Geology."

basis of the figures in the "Nautical Almanack" by which every ship sails, — are difficult and abstract enough, as most of us found to our cost in our youth.

There is no doubt a strong tendency to revolt against abstract reasoning: human nature has a strong "factish" element in it. The reasonings of the "Principia" are now accepted; but in the beginning they were "mere crotchets of Mr. Newton's," — Flamsteed, the greatest astronomical discoverer of his day, the man of facts *par excellence*, so called them. They have irresistibly conquered; but at first even those most conversant with the matter did not believe them. I do not claim for the conclusions of English political economy the same certainty as for the laws of motion; but I say that the method by which they have been obtained is the same, and that the difference in the success of the two investigations largely comes from this, — that the laws of wealth are the laws of a most complex phenomenon which you can but passively observe, and on which you cannot try experiments for science' sake, and that the laws of motion relate to a matter on which you can experiment, and which is comparatively simple in itself.

And to carry the war into the enemy's country, I say also that the method proposed by Mr. Cohn — the "All-Case" method — is impossible. When I read the words "all the facts of English banking," I cannot but ask, Of what facts is Mr. Cohn thinking? Banking in England goes on growing, multiplying, and changing, as the English people itself goes on growing, multiplying, and changing. The facts of it are one thing to-day and another to-morrow; nor at one moment does any one know them completely. Those who best know many of them will not tell them or hint them; gradually and in the course of years they separately come to light, and by the time they do so, for the most part, another crop of unknown ones has accumulated. If we wait to reason till the

"facts" are complete, we shall wait till the human race has expired. I think that Mr. Cohn, and those who think with him, are too "bookish" in this matter: they mean, by "having all the 'facts' before them," having all the printed facts, all the statistical tables; but what has been said of nature is true of commerce: — "Nature," says Sir Charles Lyell, "has made it no part of her concern to provide a record of her operations for the use of men;" nor does trade either, — only the smallest of fractions of actual transactions is set down so that investigation can use it. Literature has been called the "fragment of fragments"; and in the same way statistics are the "scrap of scraps." In real life scarcely any one knows more than a small part of what his neighbor is doing, and he scarcely makes public any of that little, or of what he does himself. A complete record of commercial facts, or even of one kind of such facts, is the completest of dreams; you might as well hope for an entire record of human conversation.

There is also a second antagonistic method to that of English political economy, which by contrast I will call the "Single-Case" method. It is said that you should analyze each group of facts separately; that you should take the panic of 1866 separately, and explain it; or at any rate, the whole history of Lombard Street separately, and explain it. And this is very good and very important, but it is no substitute for a preliminary theory: you might as well try to substitute a corollary for the proposition on which it depends. The history of a panic is the history of a confused conflict of many causes; and unless you know what sort of effect each cause is likely to produce, you cannot explain any part of what happens, — it is trying to explain the bursting of a boiler without knowing the theory of steam. Any history of similar phenomena like those of Lombard Street could not be usefully told unless there was a considerable accumulation of applicable doctrine before

existing: you might as well try to write the "life" of a ship, making as you went along the theory of naval construction, — clumsy dissertations would run all over the narrative, and the result would be a perfect puzzle.

I have been careful not to use in this discussion of methods the phrase which is oftenest used, viz., the "Historical" method, because there is an excessive ambiguity in it. Sometimes it seems what I have called the "Enumerative" or "All-Case" method, sometimes the "Single-Case" method, a most confusing double meaning, for by the mixture of the two the mind is prevented from seeing the defects of either; and sometimes it has other meanings, with which, as I shall show, I have no quarrel, but rather much sympathy. Rightly conceived, the Historical method is no rival to the abstract method rightly conceived; but I shall be able to explain this better and less tediously at the end of these papers than I can at the beginning.

This conclusion is confirmed by a curious circumstance: at the very moment that our political economy is objected to in some quarters as too abstract, in others an attempt is made to substitute for it one which is more abstract still. Mr. Stanley Jevons, and M. Walras of Lausanne, without communication and almost simultaneously, have worked out a "mathematical" theory of political economy; and any one who thinks what is ordinarily taught in England objectionable because it is too little concrete in its method, and looks too unlike life and business, had better try the new doctrine, which he will find to be much worse on these points than the old.

But I shall be asked, Do you then say that English political economy is perfect? Surely it is contrary to reason that so much difficulty should be felt in accepting a real science properly treated. At the first beginning, no doubt, there are difficulties in gaining a hearing for all sciences; but English political

economy has long passed out of its first beginning: surely, if there were not some intrinsic defect, it would have been firmly and coherently established, just as others are.

In this reasoning there is evident plausibility; and I answer that in my judgment, there are three defects in the mode in which political economy has been treated in England, which have prevented people from seeing what it really is and from prizing it at its proper value.

First. It has often been put forward, not as a theory of the principal causes affecting wealth in *certain* societies, but as a theory of the principal, sometimes even of all, the causes affecting wealth in *every* society; and this has occasioned many and strong doubts about it. Travelers fresh from the sight and historians fresh from the study of peculiar and various states of society, look with dislike and disbelief on a single set of abstract propositions which claim, as they think, to be applicable to all such societies, and to explain a most important part of most of them. I cannot here pause to say how far particular English economists have justified this accusation; I only say that taking the whole body of them, there is much ground for it, and that in almost every one of them there is some ground. No doubt almost every one—every one of importance—has admitted that there is a "friction" in society which counteracts the effect of the causes treated of: but in general they leave their readers with the idea that after all, this friction is but subordinate; that probably in the course of years it may be neglected; and at any rate, that the causes assigned in the science of political economy, as they treat it, are the main and principal ones. Now, I hold that these causes are only the main ones in a single kind of society,—a society of grown-up competitive commerce, such as we have in England; that it is only in such societies that the other and counteracting

forces can be set together under the minor head of "friction," but that in other societies these other causes — in some cases one and in some another — are the most effective ones, and that the greatest confusion arises if you try to fit on *un*economical societies the theories only true of, and only proved as to, economical ones. In my judgment we need, not that the authority of our political economy should be impugned, but that it should be *minimized;* that we should realize distinctly where it is established, and where not; that its sovereignty should be upheld, but its frontiers marked: and until this is done, I am sure that there will remain the same doubt and hesitation in many minds about the science that there is now.

Secondly. I think in consequence of this defect of conception, economists have been far more abstract, and in consequence much more dry, than they need have been. If they had distinctly set before themselves that they were dealing only with the causes of wealth in a single set of societies, they might have effectively pointed their doctrines with facts from those societies; but so long as the vision of universal theory vaguely floated before them, they shrank from particular illustrations. Real societies are plainly so many and so unlike that an instance from one kind does not show that the same thing exists in other societies, — it rather raises in the mind a presumption that it does not exist there; and therefore speculators aiming at an all-embracing doctrine refrain from telling cases, because those cases are apt to work in unexpected ways, and to raise up the image not only of the societies in which the tenet illustrated is true, but also of the opposite group in which it is false.

Thirdly. It is also in consequence, as I imagine, of this defective conception of their science, that English economists have not been as fertile as they should have been in verifying it. They have been too content to remain in the "abstract," and to shrink

from concrete notions, because they could not but feel that many of the most obvious phenomena of many nations did not look much like their abstractions: whereas in the societies with which the science is really concerned, an almost infinite harvest of verification was close at hand, ready to be gathered in; and because it has not been used, much confidence in the science has been lost, and it is thought "to be like the stars, which give no good light because they are so high."

Of course this reasoning implies that the boundaries of this sort of political economy are arbitrary, and might be fixed here or there; but this is already implied when it is said that political economy is an abstract science. All abstractions are arbitrary: they are more or less convenient fictions made by the mind for its own purposes. An abstract idea means a concrete fact or set of facts *minus* something thrown away. The fact or set of facts were made by nature; but how much you will throw aside of them and how much you will keep for consideration you settle for yourself. There may be any number of political economies, according as the subject is divided off in one way or in another; and in this way all may be useful if they do not interfere with one another, or attempt to rule further than they are proved.

The particular political economy which I have been calling the "English political economy" is that of which the first beginning was made by Adam Smith; but what he did was much like the rough view of the first traveler who discovers a country, — he saw some great outlines well, but he mistook others and left out much. It was Ricardo who made the first map; who reduced the subjects into consecutive shape, and constructed what you can call a science. Few greater efforts of mind have been made, and not many have had greater fruits. From Ricardo the science passed to a whole set of minds, — James Mill,

Senior, Torrens, MacCulloch, and others, who busied themselves with working out his ideas, with elaborating and with completing them. For five-and-twenty years the English world was full of such discussions. Then Mr. J. S. Mill — the Mr. Mill whom the present generation know so well, and who has had so much influence — shaped with masterly literary skill the confused substance of those discussions into a compact whole. He did not add a great deal which was his own, and some of what is due to him does not seem to me of great value; but he pieced the subjects together, showed where what one of his predecessors had done had fitted on to that of another, and adjusted this science to other sciences according to the notions of that time. To many students his book is the Alpha and Omega of political economy; they know little of what was before, and imagine little which can come after in the way of improvement. But it is not given to any writer to occupy such a place: Mr. Mill would have been the last to claim it for himself; he well knew that taking his own treatise as the standard, what he added to political economy was not a ninth of what was due to Ricardo, and that for much of what is new in his book he was rather the *secrétaire de la rédaction*, expressing and formulating the current views of a certain world, than producing by original thought from his own brain. And his remoteness from mercantile life, and I should say his enthusiastic character, eager after things far less sublunary than money, made him little likely to give finishing touches to a theory of "the great commerce." In fact, he has not done so: much yet remains to be done in it, as in all sciences. Mr. Mill, too, seems to me open to the charge of having widened the old political economy either too much or not enough. If it be, as I hold, a theory proved of and applicable to particular societies only, much of what is contained in Mr. Mill's book should not be there; if it is, on the contrary, a theory

holding good for all societies as far as they are concerned with wealth, much more ought to be there, and much which is there should be guarded and limited. English political economy is not a finished and completed theory, but the first lines of a great analysis which has worked out much, but which still leaves much unsettled and unexplained.

There is nothing capricious, we should observe, in this conception of political economy; nor, though it originated in England, is there anything specially English in it. It is the theory of commerce, as commerce tends more and more to be when capital increases and competition grows. England was the first — or one of the first — countries to display these characteristics in such vigor and so isolated as to suggest a separate analysis of them; but as the world goes on, similar characteristics are being evolved in one society after another. A similar money market, a similar competing trade based on large capital, gradually tends to arise in all countries. As "men of the world" are the same everywhere, so the great commerce is the same everywhere. Local peculiarities and ancient modifying circumstances fall away in both cases; and it is of this one and uniform commerce, which grows daily, and which will grow, according to every probability, more and more, that English political economy aspires to be the explanation.

And our political economy does not profess to prove this growing world to be a good world, far less to be the best. Abroad, the necessity of contesting socialism has made some writers use the conclusions brought out by our English science for that object; but the aim of that science is far more humble, — it says, "These and these forces produce these and these effects," and there it stops. It does not profess to give a moral judgment on either; it leaves it for a higher science, and one yet more difficult, to pronounce what ought and what ought not to be.

The first thing to be done for English political economy, as I hold, is to put its aim right. So long as writers on it do not clearly see, and as readers do not at all see, the limits of what they are analyzing, the result will not satisfy either. The science will continue to seem what to many minds it seems now, —proved, perhaps, but proved *in nubibus;* true, no doubt, somehow and somewhere, but that somewhere a *terra incognita*, and that somehow an unknown quantity. As a help in this matter, I propose to take the principal assumptions of political economy one by one, and to show — not exhaustively, for that would require a long work, but roughly — where each is true and where it is not. We shall then find that our political economy is not a questionable thing of unlimited extent, but a most certain and useful thing of limited extent. By marking the frontier of our property we shall learn its use, and we shall have a positive and reliable basis for estimating its value.

I.—THE TRANSFERABILITY OF LABOR.

The first assumption which I shall take is that which is perhaps oftener made in our economical reasonings than any other; namely, that labor (masculine labor, I mean) and capital circulate readily within the limits of a nation from employment to employment, leaving that in which the remuneration is smaller and going to that in which it is greater. No assumption can be better founded as respects such a country as England, in such an economical state as our present one. A rise in the profits of capital in any trade brings more capital to it with us nowadays — I do not say quickly, for that would be too feeble a word, but almost instantaneously. If owing to a high price of corn the corn trade on a sudden becomes more profitable than usual, the bill cases of bill-brokers and bankers are in a few days stuffed with corn bills; that is to say, the free capital of the country is, by the lending capitalists, the bankers and bill-brokers, transmitted where it is most wanted. When the price of coal and iron rose rapidly a few years since, so much capital was found to open new mines and to erect new furnaces that the profits of the coal and iron trades have not yet recovered it. In this case the influence of capital attracted by high profits was not only adequate, but much more than adequate; instead of reducing these profits only to an average level, it reduced them below that level: and this happens commonly, for the speculative enterprise which brings in the new capital is a strong, eager, and rushing force, and rarely stops exactly where it should. Here and now a craving for capital in a

trade is almost as sure to be followed by a plethora of it as winter to be followed by summer. Labor does not flow so quickly from pursuit to pursuit, for man is not so easily moved as money; but still it moves very quickly. Patent statistical facts show what we may call "the tides" of our people. Between the years shown by the last census[es], the years 1861 and 1871, the population of—

The Northern counties	increased	23	per cent.
Yorkshire	"	19	"
Northwestern counties	"	14	"
London	"	16	"

While that of—

The Southwestern counties	only increased	2	per cent.
Eastern	"	7	"
North Midland	"	9	"

though the fertility of marriages is equal. The set of labor is steadily and rapidly from the counties where there is only agriculture and little to be made of new labor, towards those where there are many employments and where much is to be made of it.

No doubt there are, even at present in England, many limitations to this tendency, both of capital and of labor, which are of various degrees of importance, and which need to be considered for various purposes; there is a "friction": but still it is only a "friction"; its resisting power is mostly defeated, and at a first view need not be regarded. But taking the world, present and past, as a whole, the exact contrary is true: in most ages and countries this tendency has been not victorious but defeated; in some cases it can scarcely be said even to have existed, much less to have conquered. If you take at random a country in history, the immense chances are that you will find this tendency either to be altogether absent, or not at all to prevail as it does with us now. This primary assumption of our political economy is

not true everywhere and always, but only in a few places and a few times.

The truth of it depends on the existence of conditions which, taken together, are rarely satisfied. Let us take labor first, as it is the oldest and simplest of the two. First, there must be "employments" between which labor is to migrate; and this is not true at all of the primitive states of society. We are used to a society which abounds in felt wants that it can satisfy, and where there are settled combinations of men — trades, as we call them — each solely occupied in satisfying some one of them; but in primitive times nothing at all like this exists, — the conscious wants of men are few, the means of supplying them still fewer, and the whole society homogeneous, one man living much as another. Civilization is a shifting mixture of many colors; but barbarism was and is of a dull monotony, hardly varying even in shade.

A picture or two of savage tribes brings this home to the mind better than abstract words. Let us hear Mr. Catlin's description of a favorite North-American tribe, with which he means us to be much pleased: —

"The Mandans, like all other tribes, live lives of idleness and leisure; and of course devote a great deal of time to their sports and amusements, of which they have a great variety. Of these dancing is one of the principal, and may be seen in a variety of forms; such as the buffalo dance, the boasting dance, the begging dance, the scalp dance, and a dozen other kinds of dances, all of which have their peculiar characters and meanings or objects."*

Then he describes the "starts and jumps" of these dances, and goes on: —

"Buffaloes, it is known, are a sort of roaming creatures congregating occasionally in huge masses, and strolling away about the country from east to west or from north to south, or just where their whims or strange fancies may lead them; and the Mandans are sometimes by this means most unceremoniously left

* "North-American Indians," Letter 18.

without anything to eat, and being a small tribe, and unwilling to risk their lives by going far from home in the face of their more powerful enemies, are oftentimes left almost in a state of starvation. In any emergency of this kind, every man musters and brings out of his lodge his mask (the skin of a buffalo's head with the horns on), which he is obliged to keep in readiness for this occasion; and then commences the buffalo dance of which I have spoken, which is held for the purpose of making 'buffalo come,' as they term it, — of inducing the buffalo herds to change the direction of their wanderings, and bend their course towards the Mandan village and graze about on the beautiful hills and bluffs in its vicinity, where the Mandans can shoot them down and cook them as they want them for food.

"For the most part of the year the young warriors and hunters, by riding out a mile or two from the village, can kill meat in abundance; and sometimes large herds of these animals may be seen grazing in full view of the village. There are other seasons also when the young men have ranged about the country as far as they are willing to risk their lives on account of their enemies, without finding meat. This sad intelligence is brought back to the chiefs and doctors, who sit in solemn council and consult on the most expedient measures to be taken, until they are sure to decide upon the old and only expedient which never has failed."

This is the buffalo dance, which is incessantly continued till "buffalo come," and which the whole village by relays of dancers keeps up in succession. And when the buffaloes are seen,

"there is then a brisk preparation for the chase; a grand hunt takes place; the choicest pieces of the victims are sacrificed to the Great Spirit, and then a surfeit and a carouse. These dances have sometimes been continued in this village two and three weeks without stopping an instant, until the joyful moment when buffaloes made their appearance. So they '*never fail*,'"*

as the village thinks, to bring the buffaloes in.

Such is the mode of gaining the main source of existence, without which the tribe would starve. And as to the rest, we are told: — "The principal occupations of the women in this village consist in procuring wood and water, in cooking, dressing robes and

* Same letter. The text is a jumble of Bagehot, Catlin, and blunders. — Ed.

other skins, in drying meat and wild fruit, and raising corn (maize)."*

In this attractive description there is hardly any mention of male labor at all; the men hunt, fight, and amuse themselves, and the women do all the rest.

And in the lowest form of savage life, in the Stone Age, the social structure must have been still more uniform, for there were still less means to break or vary it. The number of things which can be made with a flint implement is much greater than one would have imagined, and savages made more things with it than any one would make now; time is nothing in the savage state, and protracted labor, even with the worst instrument, achieves much, especially when there are no other means of achieving anything: but there is no formal division of employments, — no cotton trade, no iron trade, no woolen trade. There are beginnings of a division, of course; but as a rule, every one does what he can at everything.

In much later times the same uniformity in the structure of society still continues. We all know from childhood how simple is the constitution of a pastoral society: as we see it in the Pentateuch, it consists of one family, or a group of families, possessing flocks and herds, on which and by which they live; they have no competing employments, no alternative pursuits. What manufactures there are, are domestic, are the work of women at all times, and of men — of certain men — at spare times. No circulation of labor is then conceivable, for there is no circle; there is no group of trades round which to go, for the whole of industry is one trade.

Many agricultural communities are exactly similar. The pastoral communities have left the life of movement, which is essential to a subsistence on the flocks and herds, and have fixed themselves on the soil; but they have hardly done more than change one sort of

* Letter 17.

uniformity for another. They have become peasant proprietors, — combining into a village, and holding more or less their land in common, but having no pursuit worth mentioning except tillage; the whole of their industrial energy — domestic clothes-making and similar things excepted — is absorbed in that.

No doubt in happy communities a division of labor very soon and very naturally arises, and at first sight we might expect that with it a circulation of labor would begin too: but an examination of primitive society does not confirm this idea; on the contrary, it shows that a main object of the social organization which then exists, is to impede or prevent that circulation. And upon a little thought the reason is evident. There is no paradox in the notion: early nations were not giving up an advantage which they might have had; the good which we enjoy from the circulation of labor was unattainable by them; all they could do was to provide a substitute for it, — a means of enjoying the advantages of the division of labor without it, — and this they did. We must carry back our minds to the circumstances of primitive society before we can comprehend the difficulty under which they labored, and see how entirely it differs from any which we have to meet now.

A free circulation of labor from employment to employment involves an incessant competition between man and man, which causes constant quarrels, — some of which, as we see in the daily transactions of trades-unions, easily run into violence; and also a constant series of new bargains, one differing from another, some of which are sure to be broken or said to be so, which makes disputes of another kind. The peace of society was exposed in early times to greater danger from this source than now, because the passions of men were then less under control than now. In the "simple and violent times," as they have been well called, "which we read of in our Bibles," people struck one another and people killed one

another for very little matters, as we should think them; and the most efficient counteractive machinery which now preserves that peace, then did not exist. We have now in the midst of us a formed, elaborate, strong government, which is incessantly laying down the best rules which it can find to prevent trouble under changing circumstances, and which constantly applies a sharp pervading force running through society to prevent and punish breaches of those rules. We are so familiar with the idea of a government inherently possessing and daily exercising both executive and legislative power, that we scarcely comprehend the possibility of a nation existing without them; but if we attend to the vivid picture given in the Book of Judges of an early stage in Hebrew society, we shall see that there was then absolutely no legislative power, and only a faint and intermittent executive power. The idea of law-making, the idea of making new rules for new circumstances, would have been as incomprehensible to Gideon or Abimelech as the statutes at large to a child of three years old. They and their contemporaries thought that there was an unalterable law, consecrated by religion and confirmed by custom, which they had to obey; but they could not have conceived an alteration of it except as an act of wickedness, — a worshiping of Baal. And the actual coercive power available for punishing breaches of it was always slight, and often broken: one "judge" or ruler arises after another, sometimes [one] in one tribe and place and another in another, and exercises some kind of jurisdiction, but his power is always limited; there is no organization for transmitting it, and often there is no such person, — no king in Israel whatever.

The names and the details of this book may or may not be historical, but its spirit is certainly true. The peace of society then reposed on a confused sentiment, in which respect for law as such — at least law in our usual modern sense — was an inconsiderable

element, and of which the main components were a coercive sense of ingrained usage, which kept men from thinking what they had not before thought and from doing what they had not before done; a vague horror that something, they did not well know what, might happen if they did so; a close religion which filled the air with deities who were known by inherited tradition, and who hated uninherited ways; and a submission to local opinion inevitable when family and tribe were the main props of life, — when there really was "no world without Verona's walls,"* — when every exile was an outcast, expelled from what was then most natural, and scarcely finding an alternative existence.

No doubt this sentiment was in all communities partially reinforced by police; even at the time of the "Judges" there were no doubt "local authorities," as we should now say, who forcibly maintained some sort of order even when the central power was weakest. But the main support of these authorities was the established opinion: they had no military to call in, no exterior force to aid them; if the fixed sentiment of the community was not strong enough to aid them, they collapsed and failed. But that fixed sentiment would have been at once weakened, if not destroyed, by a free circulation of labor, which is a spring of progress that is favorable to new ideas, that brings in new inventions, that prevents the son being where his father was, that interrupts the tradition of generations and breaks inherited feeling. Besides causing new sorts of quarrels by creating new circumstances and new occasions, this change of men from employment to employment decomposes the moral authority which alone in this state of society can prevent quarrels or settle them. Accordingly, the most successful early societies have forbidden this ready change as much as possible, and have endeavored as far as they could to obtain the

*"Romeo and Juliet," iii. 3.

advantages of the division of labor without it. Sir Henry Maine, to whom this subject so peculiarly belongs, and who has taught us so much more on it than any one else, shall describe the industrial expedients of primitive society as he has seen them still surviving in India: —

"There is," he says, "yet another feature of the modern Indian cultivating groups which connects them with primitive Western communities of the same kind. I have several times spoken of them as organized and self-acting; they in fact include a nearly complete establishment of occupations and trades for enabling them to continue their collective life without assistance from any person or body external to them. Besides the headman or council, exercising quasi-judicial, quasi-legislative power, they contain a village police, now recognized and paid in certain provinces by the British government. They include several families of hereditary traders, — the blacksmith, the harness-maker, the shoemaker. The Brahmin is also found for the performance of ceremonies, and even the dancing-girl for attendance at festivities. There is invariably a village accountant, — an important personage among an unlettered population; so important, indeed, and so conspicuous, that according to reports current in India, the earliest English functionaries engaged in settlements of land were occasionally led, by their assumption that there must be a single proprietor somewhere, to mistake the accountant for the owner of the village, and to record him as such in the official register. But the person practicing any one of these hereditary employments is really a servant of the community as well as one of its component members. He is sometimes paid by an allowance in grain, more generally by the allotment to his family of a piece of cultivated land in hereditary possession. Whatever else he may demand for the wares he produces, is limited by a customary standard of price, very rarely departed from."*

To no world could the free circulation of labor, as we have it in England and as we assume it in our political economy, be more alien, and in none would it have been more incomprehensible. In this case as in many others, what seems in later times the most natural organization is really one most difficult to

*"Village Communities," Lecture iv.

create, and it does not arise till after many organizations which seem to our notions more complex have preceded it and perished. The village association of India, as Sir Henry Maine describes it, seems a much more elaborate structure, a much more involved piece of workmanship, than a common English village where every one chooses his own calling, and where there are no special rules for each person, and where a single law rules all; but in fact our organization is the more artificial, because it presupposes the pervading intervention of an effectual government, — the last triumph of civilization, and one to which early times had nothing comparable. In expecting what we call "simple things" from early ages, we are in fact expecting them to draw a circle without compasses, to produce the results of civilization when they have not attained civilization.

One instance of this want of simplicity in early institutions which has, almost more than any other, impaired the free transit of labor, is the complexity of the early forms of landholding. In a future page I hope to say something of the general effects of this complexity, and to compare it with the assumptions as to ownership in land made by Ricardo and others; I am here only concerned with it as affecting the movement of men, but in this respect its effect has been incalculable. As is now generally known, the earliest form of land-owning was not individual holding, but tribal owning. In the old contracts of Englishmen with savages, nothing was commoner than for the king or chief to sell tracts of land; and the buyers could not comprehend that according to native notions he had no right to do so, that he could not make a title to it, and that according to those notions there was no one who could. Englishmen in all land dealings looked for some single owner, or at any rate some small number of owners, who had an exceptional right over particular pieces of land; they could not conceive the supposed ownership of a

tribe as in New Zealand, or of a village in India, over large tracts. Yet this joint-stock principle is that which has been by far the commonest in the world, and that which the world began with; and not without good reason. In the early ages of society, it would have been impossible to maintain the exclusive ownership of a few persons in what seems at first sight an equal gift to all, a thing to which every one has the same claim. There was then no distinct government, apart from and above the tribe, any more than among New-Zealanders now; there was no compulsory agency which could create or preserve exclusive ownership of the land, even if it had been wished: and of course it could not have been wished, —for though experience has now conclusively shown that such exclusive ownership is desirable for and beneficial to the nation as a whole, as well as to the individual owner, no theorist would have been bold enough to predict this beforehand. This monopoly is almost a paradox after experience, and it would have seemed monstrous folly before it. Indeed, the idea of a discussion of it is attributing to people in the year 1000 B. C. the notions of people in the year 1800 A. D. Common ownership was then irremediable and inevitable; no alternative for it was possible, or would then have been conceivable: but it is in its essence opposed to the ready circulation of labor. Few things fix a man so much as a share in a property which is fixed by nature; and common ownership, wherever it prevails, gives the mass of men such a share.

And there is another force of the same tendency which does not act so widely, but which when it does act is even stronger, — in many cases is omnipotent; this is the disposition of many societies to crystallize themselves into *specialized* groups, which are definite units, each with a character of its own, and are more or less strictly hereditary. Sir Henry Maine has described to us how in an Indian

village the blacksmith is hereditary, and the harness-maker, and the shoemaker; and this is natural, for every trade has its secrets, which make a kind of craft or "mystery" of it, and which must be learnt by transmission or not at all. The first and most efficient kind of apprenticeship is that by birth: the father teaches his son that by which he makes his living, almost without knowing it; the son picks up the skill which is in the air of the house, almost without feeling that he is doing so. Even now we see that there are city families, and university and legal families,—families where a special kind of taste and knowledge are passed on in each generation by tradition, and which in each have in that respect an advantage over others. In most ages most kinds of skilled labor have shown a disposition to intensify this advantage by combination,—to form a bounded and exclusive society, guild, trades-union, or whatever it may be called, which keeps or tries to keep in each case to itself the rich secret of the inherited art; and even when no pains are taken, each special occupation, after it gains a certain size, tends to form itself into a separate group. Each occupation has certain peculiar characteristics which help to success in it, and which therefore it fosters and develops; and in a subtle way these traits collect together and form a group character analogous to a national character. The process of caste-making is often thought to be an old-world thing which came to an end when certain old castes were made and fixed, before the dawn of history; but in fact the process has been actively at work in recent times, and has hardly yet died out. Thus in Cashmere, where the division of castes is already minute, Mr. Drew tells us that of the Batals—a class at the very bottom of the scale,

"Whose trade it is to remove and skin carcases, and to cure leather"—he has heard that "there are two classes; . . . so apt are communities in India to divide and to subdivide, to perpetuate differences, and to separate rather than amalgamate. The higher

Batals follow the Mohammedan rules as to eating, and are allowed into some fellowship with the other Mohammedans. The lower Batals eat carrion, and would not bear the name of Musalmàn in the lips of others, though they might call themselves so." *

Just so, Mr. Hunter says that—

"The Brahmans of Lower Bengal bore to the Brahmans of Oudh the same relation that the landed gentry of Canada or Australia bears to the landed gentry of England. Each is an aristocracy, both claim the title of Esquire, but each is composed of elements whose social history is widely different, and the home aristocracy never regards the successful settlers as equal in rank. The Brahmans of the Middle Land went further: they declared the Brahmans of Lower Bengal inferior not only in the social scale, but in religious capabilities. To this day many of the north-country Brahmans do not eat with the Brahmans of the Lower Valley; and convicted felons from the Northwest will suffer repeated floggings in jail, for contumacy, rather than let rice cooked by a Bengal Brahman pass their lips." †

Caste-making is not a rare act, but a constantly occurring act, when circumstances aid it and when the human mind is predisposed to it.

One great aid to this process is the mutual animosity of the different groups. "What one nation hates," said Napoleon, "is another nation;" just so, what one caste hates is another caste: the marked characteristics of each, being different, form a certain natural basis for mutual dislike. There is an intense disposition in the human mind—as you may see in any set of schoolboys—to hate what is unusual and strange in other people; and each caste supplies those adjoining it with a conspicuous supply of what is unusual. And this hatred again makes each caste more and more unlike the other; for every one wishes as much as possible to distinguish himself from the neighboring hated castes by excelling in the peculiarities of his own caste, and by avoiding theirs.

* Frederick Drew, "Jummoo and Kashmir Territories," Chap. viii.
† W. W. Hunter, "Annals of Rural Bengal," Chap. iii.

In the ancient parts of the world, these contrasts of group to group are more or less connected for the most part with contrasts of race. Very often the origin of the caste — the mental tendency which made its first members take to its special occupation — was some inborn peculiarity of race; and at other times, as successive waves of conquest passed over the country, each race of conquerors connected themselves most with, and at last were absorbed in, the pre-existing kind of persons which they most resembled, and frequently in so doing hardened into an absolute caste what was before a half-joined and incipient group.

Each conquest, too, tends to make a set of outcasts, generally from the worst part of the previous population; and these become "hewers of wood and drawers of water"* to the conquerors, — that is, they are an outlying and degraded race, which is not admitted to compete or mix with the others, and which becomes more degraded from feeling that it is thus inferior, and from being confined to the harder, baser, and less teaching occupations; and upon these unhappy groups the contempt and hatred of the higher ones tend to concentrate themselves, and like most strong sentiments in the early world, these feelings find for themselves a religious sanction. To many villages in India, Sir Henry Maine says, there are attached a class of "outsiders" who "never enter the village, or only enter reserved portions of it," who "are looked upon as essentially impure," whose very "touch is avoided as contaminating."* These poor people are more or less thought to be "accursed"; to have some taint which shows that the gods hate them, and which justifies men in hating them too and in refusing to mix with them.

The result of these causes is, that many ancient societies are complex pieces of patchwork; bits of contrasted human nature, put side by side. They

* "Village Communities," Lecture iv.

have a variegated complexity, which modern civilized states mostly want. And there must clearly have been an advantage in this organization of labor, — to speak of it in modern phrase, — though it seems to us now so strange ; or it would not have sprung up independently in many places and many ages, and have endured in many for long tracts of years. This advantage, as we have seen, was the gain of the division of labor without the competition which with us accompanies it, but which the structure of society was not then hard enough to bear.

No doubt we must not push too far this notion of the rigidity of caste : the system was too rigid to work without some safety-valves, and in every age and place where that system prevails, some have been provided. Thus in India we are told : —

"A Bráhmana unable to subsist by his own duties may live by those of a soldier ; if he cannot get a subsistence by either of these employments, he may apply to tillage and attendance on cattle, or gain a competence by traffic, avoiding certain commodities. A Kshatriya in distress may subsist by all these means, but he must not have recourse to the highest functions. . . . A Vaiśya unable to subsist by his own duties may descend to the servile acts of a S'údra ; and a S'údra, not finding employment by waiting on men of the higher classes, may subsist by handicrafts. . . . Besides the particular occupations assigned to each of the mixed classes, they have the alternative of following that profession which regularly belongs to the class from which they derive their origin on the mother's side." *

And so on, without end.

And probably it is through these supplementary provisions, as I may call them, that the system of caste ultimately breaks down and disappears. It certainly disappeared in ancient Egypt when the compact Roman government was strong enough to do without it, and when a change of religion had removed the sanctions which fixed and consecrated it. The process is most slow, as our experience in India

* Colebrooke's Essays, Vol. ii., No. vi., "Indian Classes."

proves; the saying that "La Providence a ses aises dans le temps"* has rarely elsewhere seemed so true: still, the course is sure, and the caste system will in the end pass away, whenever an efficient substitute has been made for it and the peace of industry secured without it.

But it would be a great mistake to believe that whenever and wherever there is an efficient external government capable of enforcing the law, and of making the competitive migration of labor safe and possible, such migration of itself at once begins: there is in most cases a long and dreary economical interval to be passed first. In many countries, the beginning of such migration is for ages retarded by the want of another requisite, — the want of external security. We have come in modern Europe to look on nations as if they were things indestructible, — at least on large nations; but this is a new idea, and even now it has to be taken with many qualifications. But in many periods of history it has not been true at all: the world was in such confusion that it was almost an even chance whether nations should continue, or whether they should be conquered and destroyed. In such times the whole energy of the community must be concentrated on its own defense; all that interferes with it must be sacrificed if it is to live: and the most efficient mode of defending it mostly is a feudal system, — that is, a local militia based on the land, where each occupier of the soil has certain services to render, of which he cannot divest himself, and which he must stay on certain definite fields to perform when wanted. In consequence, the races of men which were possessed of an organization easily adapting itself to the creation of such a militia have had a striking tendency to prevail in the struggle of history.

"The feudal system," says Sir George Campbell, on many accounts one of our most competent judges, "I believe to be no

* "Providence takes pleasure in time."

invention of the Middle Ages, but the almost necessary result of the hereditary character of the Indo-Germanic institutions, when the tribes take the position of dominant conquerors. They form in fact a hereditary army, with that gradation of fealty from the commander-in-chief to the private soldier which is essential in military operations. Accordingly, we find that among all the tribes of Indo-Germanic blood which have conquered and ruled Indian provinces, the tendency is to establish a feudal system extremely similar to that which prevailed in Europe: in Rajpootana the system is still in full force; the Mahrattas and Sikhs had both established a similar system; in my early days it existed in great perfection in some parts of the cis-Sutlej Sikh states."*

And where the system is most developed, at the lowest point of the scale there is always an immovable class, — serfs, *villeins regardant*, or what we choose to call them, — who do not fight themselves, who perhaps are too abject in spirit, or perhaps are of too dubious fidelity to be let have arms, but who cultivate the ground for those who really fight. The soldier class, rooted to the land by martial tenure, has beneath it a non-soldier class even more rooted to the soil by the tenure of tilling it. I need not say how completely such a system of military defense, and such a system of cultivation, are opposed to the free transit of labor from employment to employment: where these systems are perfectly developed, this transit is not so much impeded as prevented.

And there is a yet more pervading enemy of the free circulation of labor; this is slavery. We must remember that our modern notion that slavery is an exceptional institution is itself an exceptional idea: it is the product of recent times and recent philosophies; no ancient philosopher, no primitive community would have comprehended what we meant by it. That human beings are divided into strong and weak, higher and lower, or what is thought to be such, and that the weak and inferior ought to be made to serve the higher and better whether they

*"Tenure of Land in India," Chap. iii. of "Systems of Land Tenure in Various Countries" (Cobden Club Essays).

would wish to do so or not, are settled axioms of early thought. Whatever might be the origin and whatever might be the fate of other institutions, the ancient world did not doubt that slavery at all events existed "by the law of nature," * and would last as long as men. And it interferes with the ready passage of labor from employment to employment in two ways: — First, it prevents what we call for this purpose "employments" — that is, markets where labor may be bought, mostly in order that the produce may be sold. Slavery, on the contrary, strengthens and extends domestic manufactures where the produce is never sold at all, where it is never intended to be so, but where each household by its own hands makes what it wants. In a slave community so framed, not only is there little quick migration of free labor, but there are few fit places for it to migrate between, there are no centers for the purchase of much of it; society tends to be divided into self-sufficing groups, buying little from the exterior. And at a later stage of industrial progress, slavery arrests the movement of free labor still more effectively by providing a substitute: it is then the slave labor which changes occupation, and not the free labor. Just as in the present day a capitalist who wants to execute any sort of work hires voluntary labor to do it, so in a former stage of progress he would buy slaves in order to do it. He might not indeed be able to buy enough slaves — enough suitable slaves, that is — for his purpose: the organization of slavery has never been as effectual as our present classified system of free labor, and from intrinsic defects never can be; but it does develop earlier. Just when the system of free labor might develop if it were let alone, the imperfect substitute of slavery steps in and spoils it. When free labor still moves slowly and irregularly,

* "By nature some command and others obey. . . . He who can do nothing but labor with his body is . . . a slave by nature."—Aristotle's "Politics," Book i., Chap. ii. The same subject is continued in several following chapters. — Ed.

and when frequent wars supply the slave market with many prisoners, the slave market is much the easiest resource of the capitalist; so it is when a good slave trade keeps it well filled: the capitalist finds it better to buy than to hire, for there are in this condition of things comparatively many men to be bought and comparatively few to be hired. And the result takes unexpected directions. "What the printing press is in modern times," says a German writer, "that slavery was in ancient times:" and though this may be a little exaggerated, it is certain that in ancient Rome, books were produced much cheaper and in much greater number than they were for hundreds of years afterwards; when there was a demand for a book, extra copying slaves could be "turned on" to multiply it in a way which in later times, when slavery had ceased, was impossible, and which is only surpassed by the way in which additional compositors are applied to works in demand now. And political philosophers proposed to obtain revenue from this source, and to save taxation. "Suppose," says Xenophon, "that the Athenian state should buy twelve thousand* slaves, and should let them out to work in the mines at an obolus a head, and suppose that the whole amount annually thus received should be employed in the purchase of new slaves, who should again in the same way yield the same income, and so on successively: the state would then by these means in five or six years possess six thousand slaves,"† which would yield a large income. The idea of a compound-interest investment in men, though abhorrent to us, seemed most natural to Xenophon; and almost every page of the classics proves how completely the civilization then existing was based on slavery in one or other of its forms, — that of skilled labor (the father of Demosthenes owned thirty-three cutlers and twenty coach-makers), or

* Twelve *hundred*. — Ed.

† A summary (not an exact quotation) of Chap. iv. of the "Means of Increasing the Athenian Revenues." — Ed.

unskilled, that might either be worked by the proprietor or let out, as he liked. Even if this system had only economical consequences, it must have prevented the beginning of freely moving labor, for it is much handier than such a system can be at its outset; and as we know, the system has moral effects working in the same way even more powerful, for it degrades labor by making it the slave mark, and makes the free laborer — whether the *prolétaire* of ancient cities or the "mean white" of American plantations — one of the least respectable and the least workmanlike of mankind.

Happily, this full-grown form of slavery is exceedingly frail. We have ourselves seen in America how completely it collapses at an extrinsic attack, how easy it is to destroy it, how impossible to revive it; and much of the weakness of ancient civilization was also so caused. Any system which makes the mass of a society hate the constitution of that society must be in unstable equilibrium; a small touch will overthrow it, and scarcely any human power will re-establish it: and this is the necessary effect of capitalistic slavery, for it prevents all other laborers, makes slaves the "many" of the community, and fills their mind with grief and hatred. Capitalistic slavery is, as history shows, one of the easiest things to efface, as domestic slavery is one of the hardest. But capitalistic slavery has vitally influenced most of the greatest civilizations; and as domestic slavery has influenced nearly all of them, the entire effect of the two has been prodigious.

We see then that there are at least four conditions to be satisfied before this axiom of our English political economy is true within a nation: before labor can move easily and as it pleases from employment to employment, there must be such employments for it to move between; there must be an effectual government, capable of maintaining peace and order during the transition, and not requiring itself to be

supported by fixity of station in society, as so many governments have been; the nation must be capable of maintaining its independent existence against other nations, without a military system dependent on localized and immovable persons; and there must be no competing system of involuntary labor, limiting the number of employments or moving between them more perfectly than contemporary free labor. These are not indeed all the conditions needful for the truth of the axiom; but the others can be explained better when some other matters have been first discussed.

II. — THE TRANSFERABILITY OF CAPITAL.

In my last paper I discussed the fundamental principle of English political economy, — that within the limits of a nation, labor migrates from employment to employment, as increased remuneration attracts or decreased remuneration repels it; and now I have to treat the corresponding principle as to capital, — that it flows or tends to flow to trades of which the profits are high, that it leaves or tends to leave those in which the profits are low, and that in consequence there is a tendency — a tendency limited and contracted, but still a tendency — to an equality of profits through commerce.

First, this requires such a development of the division of labor as to create what we call "trade," — that is to say, a set of persons working for the wants of others, and providing for their own wants by the return commodities received from those others; but this development has only been gradually acquired by the human race. Captain Cook found some Australian tribes to whom the idea of traffic seemed unknown: they received what was given them readily, but they received it as a present only, — they seemed to have no notion of giving anything in lieu of it; the idea of barter — an idea usually so familiar to the lower races of men — appeared never to have dawned on these very low ones. But among races in such a condition there is no change of trades as capital becomes more and more profitable in any one; the very conception comes long after. Every one works for himself at everything, and he always works most at what he likes most for the time; as he changes

his desires, so far as he can he changes his labor; whenever he works he uses the few tools he has — the stone implements, the charred wood, the thongs of hide, and other such things — in the best way he can. A hundred savages are doing so at once, — some in one way, some in another, — and these are no doubt "shiftings of capital"; but there is no computation of profit, as we now reckon profit, on such shiftings. Profit, as we calculate, means that which is over after the capital is replaced; but a savage incapable of traffic does not make this calculation as to his flints and his hides, — the idea could not even be explained to him.

Secondly, this comparison requires a medium in which the profits can be calculated; that is, a *money*. Supposing that in the flax trade profits are 5 per cent., and that side by side in the cotton trade they are 15 per cent., capital will nowadays immediately run from one to the other; and it does so because those who are making much try to get more capital, and those who are making little — still more those who are losing — do not care to keep as much as they have: but if there is no money to compute in, neither will know what they are making, and therefore the process of migration wants its motive and will not begin. The first sign of extra profit in a trade — not a conclusive, but a strongly presumptive one — is an extra high price in the article that trade makes or sells; but this test fails altogether when there is no "money" to sell in. And the debit side of the account, the cost of production, is as difficult to calculate when there is no common measure between its items, or between the product and any of them. Political economists have indeed an idea of "exchangeable value," — that is, of the number of things which each article will exchange for, — and they sometimes suppose a state of barter in which people had this notion, and in which they calculated the profit of a trade by deducting the exchangeable value of the labor and

commodities used in its production from the value of the finished work; but such a state of society never existed in reality. No nation which was not clever enough to invent a money was ever able to conceive so thin and hard an idea as "exchangeable value"; even now Mr. Fawcett justly says that it puzzles many people, and sends them away frightened from books on political economy. In fact, it is an ideal which those used to money prices have framed to themselves; they see that the price of anything, the money it fetches, is equal to its "purchasing power" over things, and by steadily attending they come to be able to think of this "purchasing power" separately, and to call [it], and reason upon it as, "exchangeable value": but the idea is very treacherous even to skilled minds, and even nowadays not the tenth part of any population could ever take it in. As for the nations really in a state of barter ever comprehending it, no one can imagine it; for they are mostly unequal to easy arithmetic, and some cannot count five. A most acute traveler thus describes the actual process of bargaining among savage nations as he saw it:—

"In practice," Mr. Galton tells us of the Damaras, "whatever they may possess in their language, they certainly use no numeral greater than three; when they wish to express four they take to their fingers, which are to them as formidable instruments of calculation as a sliding rule is to an English schoolboy. They puzzle very much after five, because no spare hand remains to grasp and secure the fingers that are required for 'units.' Yet they seldom lose oxen: the way in which they discover the loss of one is not by the number of the herd being diminished, but by the absence of a face they know. When bartering is going on, each sheep must be paid for separately. Thus, suppose two sticks of tobacco to be the rate of exchange for one sheep, it would sorely puzzle a Damara to take two sheep and give him four sticks. I have done so, and seen a man first put two of the sticks apart, and take a sight over them at one of the sheep he was about to sell. Having satisfied himself that that one was honestly paid for, and finding to his surprise that exactly two sticks remained in hand to settle the account

for the other sheep, he would be afflicted with doubts : the transaction seemed to come out too 'pat' to be correct, and he would refer back to the first couple of sticks, and then his mind got hazy and confused, and wandered from one sheep to the other, and he broke off the transaction until two sticks were put into his hand and one sheep driven away, and then the other two sticks given him and the second sheep driven away."*

Such a delineation of primitive business speaks for itself ; and it is waste of space showing further that an abstraction like "value in exchange" is utterly beyond the reach of the real bartering peoples, — that a habit of using money, and of computing in it, are necessary preliminaries to comparisons of profits.

Unquestionably, the most primitive community can see if a pursuit utterly fails or if it immensely succeeds : the earliest men must have been eager in making flint tools, for there are so many of them, and no doubt they did not try to breed cattle where they died. But there was in those days no adjusted comparison between one thing and another ; all pursuits which anyhow suited went on then as they do among savages now.

Money too is in this matter essential, or all but essential, in another way : it is a form in which capital is held in *suspense* without loss. The transfer of capital from employment to employment is a matter requiring consideration ; consideration takes time, and the capital must be somewhere during that time. But most articles are bought at a risk : they lose in the process, and become second-hand ; an ordinary person cannot get rid of them without receiving for them less — often much less — than he gave. But money is never "second-hand" ; it will always fetch itself, and it loses nothing by keeping. No doubt modern civilization has invented some other forms of property which are almost as good to hold as money : some interest-bearing securities, like

*"Travels in Tropical South Africa," page 113 (Chap. v.).

Exchequer bills, are so, and pay an interest besides; but these are the creatures of money, so to say, and based upon it, — they presuppose it, and would not be possible without it. A community of pure barter, even if it could reckon and compare profits, would not be able to move capital accurately from one trade to another; for it possesses no commodity which could, without risk of loss that could not be calculated, be held idle during the computation.

The refined means by which the movement is now effected is one of the nicest marvels of our commercial civilization. The three principal of them are as follows: —

First. There is the whole of the loan fund of the country lying in the hands of bankers and bill-brokers, which moves in an instant towards a trade that is unusually profitable, if only that trade can produce securities which come within banking rules. Supposing the corn trade to become particularly good, there are immediately twice the usual number of corn bills in the bill-brokers' cases; and if the iron trade, then of iron bills. You could almost see the change of capital, if you could look into the bill cases at different times; but what you could not see is the mental skill and knowledge which have made that transfer, and without which it could not have been made safely. Probably it would be new to many people if stated plainly, but a very great many of the strongest heads in England spend their minds on little else than on thinking whether other people will pay their debts. The life of Lombard Street bill-brokers is almost exclusively so spent. Mr. Chapman, one of the partners in Overend, Gurney & Co., once rather amused a parliamentary committee by speaking with unction and enthusiasm of "paper of the very finest quality," by which he meant paper on which the best promises were written: bills of exchange are only undertakings to pay money, and the most likely to be paid are, in the market phrase, of

the "finest quality," and the less likely of inferior quality. The mind of a man like Mr. Chapman, if it could be looked into, would be found to be a graduating machine marking in an instant the rises and falls of pecuniary likelihood. Each banker in his own neighborhood is the same, — he is a kind of "solvency meter," and lives by estimating rightly the "responsibility of parties," as he would call it; and the only reason why the London bill-broker has to do it on a greater scale is, that being in the great center, he receives the surplus savings not of one district but of many, which find no means of employment there. He is thus become the greatest and most just measurer of moneyed means and moneyed probity which the world has ever seen; to reduce it to its lowest terms, he knows that more people will pay more debts than any one who now is, or ever before was, in the world. And the combined aggregate of these persons is a prepared machine ready to carry capital in any direction. The moment any set of traders want capital, the best of them, those whose promises are well known to be good, get it in a minute; because it is lying ready in the hands of those who know, and who live by knowing, that they are fit to have it.

Secondly. In modern England, there is a great speculative fund which is always ready to go into anything which promises high profits. The largest part of this is composed of the savings of men of business. When, as in 1871, the profits of many trades suddenly become much greater than usual, the Stock Exchange instantly becomes animated; there is at once a market for all kinds of securities, so long as they promise much, either by great interest or by rise of prices. Men of business who are used to a high percentage of profit in their own trade despise 3 or 4 per cent., and think that they ought to have much more; in consequence there is no money so often lost as theirs. There is an idea that it is the

country clergyman and the ignorant widow who mostly lose by bad loans and bad companies, and no doubt they often do lose: but I believe that it is oftener still, men of business of slight education and of active temperament, who have made money rapidly, and who fancy that the skill and knowledge of a special trade which have enabled them to do so will also enable them to judge of risks and measure contingencies out of that trade; whereas in fact there are no persons more incompetent, for they think they know everything when they really know almost nothing out of their little business, and by habit and nature they are eager to be doing. So much of their money as comes to London is in greater jeopardy almost than any other money; but there is a great deal which never comes there, and which those who make it are able to put out in pushing their own trade and in extending allied trades. The very defects which make the trader so bad a judge of other things make him an excellent judge of these; and he is ready and daring, and most quick to make use of what he knows. Each trade in modern commerce is surrounded by subsidiary and kindred trades, which familiarize the imagination with it and make its state known; as soon, therefore, as the conspicuous dealers in that trade are known to be doing particularly well, the people in the surrounding trades say, "Why should not we do as well too?" and they embark their capital in it, — sometimes of course wrongly, but upon the whole wisely and beneficially. In an animated business world like ours, these inroads into the trades with largest gains by the nearest parts of the speculative fund are incessant, and are a main means of equalizing profits.

Lastly. There is the obvious tendency of young men starting in business to go into the best paying business, or what is thought to be so at that time; this, in the best cases, also acts mainly on the allied and analogous trades. Little good, for the most

part, comes of persons who have been brought up on one side of the business world going quite to the other side, — of farmers' sons going to cotton spinning, or of lace-makers' sons going into shipping: each sort of trade has a tradition of its own, which is never written, probably could not be written, which can only be learned in fragments, and which is best taken in early life, before the mind is shaped and the ideas fixed. From all surrounding trades there is an incessant movement of young men with new money into very profitable trades, which steadily tends to reduce that profitableness to the common average.

I am more careful than might seem necessary to describe the entire process of equalization at length, because it is only by so doing that we can see how complex it is, and how much development in society it requires; but as yet the description is not complete, or nearly so. We have only got as far as the influx of money into new trades; but this is but a small part of what is necessary. Trades do not live by money alone; money by itself will not make anything. What then do we mean when we speak of "capital" as flowing from employment to employment?

Some writers speak as if the only thing which transfers of capital effect is a change in the sort of labor that is set in motion; and no doubt this is so far true, that all new employments of capital do require new labor. Human labor is the primitive moving force, and you must have more of it if you want more things done; but the description, though true, is most incomplete, as the most obvious facts in the matter prove. When new capital comes into cotton spinning, this means not only that new money is applied to paying cotton operatives, but also that new money is applied to buying new spinning machines; these spinning machines are made by other machines as well as labor; and the second lot of

machines again by a third set as well as other labor. In the present state of the world, nothing is made by brute labor; everything is made by aids to labor: and when capital goes from trade to trade, it settles not only which sort of labor shall be employed, but which sort of existing machines shall be first used up, which sort of new ones made, and how soon those new ones shall be worn out, not only in the selected trade, but in an endless series subsidiary to it.

To understand the matter fully, we must have a distinct view of what on this occasion and on this matter we mean by "capital." The necessity of a science like political economy is, that it must borrow its words from common life, and therefore from a source where they are not used accurately and cannot be used accurately. When we come to reason strictly on the subjects to which they relate, we must always look somewhat precisely to their meaning; and the worst is, that it will not do, if you are writing for the mass of men, even of educated men, to use words always in the same sense. Common words are so few, that if you tie them down to one meaning they are not enough for your purpose; they do their work in common life because they are in a state of incessant slight variation, meaning one thing in one discussion and another a little different in the next. If we were really to write an invariable nomenclature in a science where we have so much to say of so many things as we have in political economy, we must invent new terms, like the writers on other sciences. Mr. De Morgan said (in defense of some fresh-coined substantive), "Mathematics must not want words because Cicero did not know the differential calculus;" but a writer on political economy is bound — not perhaps by Cicero, but by his readers. He must not use words out of his own head, which they never heard of: they will not read him if he does. The best way, as we cannot do this, is to give up uniform uses, — to

write more as we do in common life, where the context is a sort of unexpressed "interpretation clause," showing in what sense words are used; only, as in political economy we have more difficult things to speak of than in common conversation, we must take more care, give more warning of any change, and at times write out the "interpretation clause" for that page or discussion, lest there should be any mistake. I know that this is difficult and delicate work; and all I have to say in defense of it is, that in practice it is safer than the competing plan of inflexible definitions. Any one who tries to express varied meanings on complex things with a scanty vocabulary of fastened senses will find that his style grows cumbrous without being accurate; that he has to use long periphrases for common thoughts; and that after all he does not come out right, for he is half his time falling back into the senses which fit the case in hand best, — and these are sometimes one, sometimes another, and almost always different from his "hard and fast" sense. In such discussions we should learn to vary our definitions as we want, just as we say "let x, y, z mean" now this and now that in different problems; and this, though they do not always avow it, is really the practice of the clearest and most effective writers.

By "capital," then, in this discussion, we mean an aggregate of two unlike sorts of artificial commodities: co-operative things which help labor, and remunerative things which pay for it. The two have this in common, that they are the produce of human labor; but they differ in almost everything else if you judge of them by the visual appearance. Between a loaf of bread and a steam engine, between a gimlet and a piece of bacon, there looks as if there were really nothing in common, except that man made both; but though the contrast of externalities is so great, the two have a most essential common property which is that which political economy fixes

upon, — the possible effect of both is to augment human wealth. Laborers work because they want bread; their work goes farther if they have good tools: and therefore economists have a common word for both tools and bread. They are both capital, and other similar things are so too.

And here we come across another of the inevitable verbal difficulties of political economy. Taking its words from common life, it finds that at times and for particular discussions it must twist them in a way which common people would never think of. The obvious resemblances which we deal with in life dictate one mode of grouping objects in the mind, and one mode of speaking of them; the latent but more powerful resemblance which science finds would dictate another form of speech and mental grouping, and then what seems a perverse use of language must be made. Thus, for the present discussion, the acquired skill of a laborer is capital, though no one in common life would call it so: it is a productive thing made by man, as much as any tool; it *is* in fact an immaterial tool, which the laborer uses just as he does a material one; it is co-operative capital as much as anything can be. And then again, the most unlikely looking and luxurious articles are "capital" if they reward and stimulate labor. Artisans like the best of rabbits, the best bits of meat, green peas, and gin; they work to get these; they would stay idle if they were not incited by these: and therefore these are "capital." Political economy (like most moral sciences) requires not only to change its definitions as it moves from problem to problem, but also for some problems to use definitions which, unless we see the motive, seem most strange; just as in acts of Parliament the necessity of the draftsman makes a very technical use of words necessary if he is to do his work neatly, and the reader will easily be most mistaken and confused if he does not heed the dictionary which such acts contain.

Remembering all this, we see at once that it is principally remunerative capital which is transferable from employment to employment. Some tools and instruments are no doubt used in many trades, especially the complex ones: knives, hammers, twine, and nails can be used, are used, in a thousand; the existing stock of these is transferred bodily when capital migrates from an employment: but in general, as I have said before, the effect of the migration on co-operative capital is to change the speed with which the existing machines are worked out, and the nature of the new machines which are made; the "live skill" of an artisan being treated as a machine. On remunerative capital the effect is simpler. As a rule, much the same commodities reward labor in different trades, and if one trade declines and another rises, the only effect is to change the laborer who gets these commodities; or if the change be from a trade which employs little skilled labor to one which employs much, then the costly commodities which skilled labor wants will be in demand, more of them will be made, and there will be an increase of animation in all the ancillary trades which help their making.

We see also more distinctly than before what we mean by an "employment": we mean a group of persons with fitting tools and of fitting skill, paid by the things they like. I purposely speak of "tools" to include all machines, even the greatest, for I want to fix attention on the fact that everything depends on the effort of man, on the primary fruit of human labor; without this to start with, all else is useless. And I use it out of brevity to include such things as coal and materials, which for any other purpose no one would call so, but which are plainly the same for what we have now to do with.

And "employment" in any large trade implies an "employer." The capitalist is the motive power in modern production, in the "great commerce." He

settles what goods shall be made, and what not; what brought to market, and what not. He is the general of the army; he fixes on the plan of operations, organizes its means, and superintends its execution. If he does this well, the business succeeds and continues; if he does it ill, the business fails and ceases: everything depends on the correctness of the unseen decisions, on the secret sagacity of the determining mind. And I am careful to dwell on this, though it is so obvious, and though no man of business would think it worth mentioning, because books forget it, — because the writers of books are not familiar with it. They are taken with the conspicuousness of the working classes: they hear them say, It is we who made Birmingham, we who made Manchester; but you might as well say that it was the "compositors" who made the *Times* newspaper. No doubt the craftsmen were necessary to both, but of themselves they were insufficient to either. The printers do not settle what is to be printed; the writers even do not settle what is to be written: it is the editor who settles everything. He creates the *Times* from day to day; on his power of hitting the public fancy its prosperity and power rest; everything depends on his daily bringing to the public exactly what the public wants to buy; the rest of Printing-House Square — all the steam presses, all the type, all the staff, clever as so many of them are — are but implements which he moves. In the very same way the capitalist edits the "business": it is he who settles what commodities to offer to the public, how and when to offer them, and all the rest of what is material. This monarchical structure of money business increases as society goes on, just as the corresponding structure of war business does, and from the same causes. In primitive times a battle depends as much on the prowess of the best fighting men, of some Hector or some Achilles, as on the good science of the general; but nowadays it is a

man at the far end of a telegraph wire — a Count Moltke, with his head over some papers — who sees that the proper persons are slain, and who secures the victory. So in commerce. The primitive weavers are separate men with looms apiece, the primitive weapon makers separate men with flints apiece; there is no organized action, no planning, contriving, or foreseeing in either trade, except on the smallest scale: but now the whole is an affair of money and management, of a thinking man in a dark office computing the prices of guns or worsteds. No doubt in some simple trades these essential calculations can be verified by several persons, — by a board of directors, or something like it; but these trades, as the sagacity of Adam Smith predicted* and as painful experience now shows, are very few: the moment there comes anything difficult or complicated, the Board "does not see its way"; and then, except it is protected by a monopoly, or something akin to monopoly, the individual capitalist beats it out of the field. But the details of this are not to my present purpose. The sole point now material is, that the transference of capital from employment to employment involves the pre-existence of employment, and this pre-existence involves that of "employers"; of a set of persons — one or many, though usually one — who can effect the transfer of that capital from employment to employment, and can manage it when it arrives at the employment to which it is taken.

And this management implies knowledge. In all cases successful production implies the power of adapting means to ends, of making what you want as you want it: but after the division of labor has arisen, it implies much more than this; it then requires too that the producer should know the wants of the consumer, — a man whom he mostly has never seen, whose name probably he does not know, very likely even speaking another language, living according to other habits, and having scarcely any point

* "Wealth of Nations," Book v., Chap. i.

of intimate relation to the producer except a liking for what he produces. And if a person who does not see is to suit another who is not seen, he must have much head knowledge, an acquired learning in strange wants as well as of the mode of making things to meet them. A person possessing that knowledge is necessary to the process of transferring capital, for he alone can use it when the time comes; and if he is at the critical instant not to be found, the change fails, and the transfer is a loss and not a gain.

This description of the process by which capital is transferred, and of what we mean by it, may seem long, but it will enable us to be much shorter in showing the conditions which that transfer implies. First, it presupposes the existence of transferable labor; and I showed before how rare transferable labor is in the world, and how very peculiar are its prerequisites. You cannot have it unless you have a strong government, which will keep peace in the delicate line on which people are moving. You must not have fixed castes in inherited occupations, which at first are ways and means to do without a strong government, but which often last on after it begins; you must not have a local army which roots men to fixed spots for military purposes, and therefore very much to fixed pursuits; and you must not have slavery, for this is an imperfect substitute for free transferable labor, which effectually prevents the existence of it. Complete freedom of capital presupposes complete freedom of labor, and can only be attained when and where this exists.

No doubt capital begins to move much before the movement of labor is perfect. The first great start of it commences with a very unpopular person, who is almost always spoken evil of when his name is mentioned, but in whom those who know the great things of which he has been the forerunner will always take a great interest; it is the money-lender in

a primitive community whose capital is first transferred readily from occupation to occupation. Suppose a new crop, say cotton, becomes suddenly lucrative; immediately the little proprietors throng to the money-lender to obtain funds to buy cotton: a new trade is begun by his help, which could not have been begun without him. If cotton ceases to be a good crop, he ceases to lend to grow it; his spare capital either remains idle or goes to some other loan, perhaps to help some other crop which has taken the place of cotton in profitableness. There is no more useful trade in early civilization, though there is none which has such a bad name; and not unnaturally, for there is none which then produces more evil as well as good. Securities for loans, such as we have them in developed commerce, are rarely to be met with in early times; the land — the best security, as we think it — is then mostly held upon conditions which prevent its being made in that way available; there is little movable property of much value, and peasants who work the land have scarcely any of that little: the only thing they can really pledge is their labor, — *themselves*. But then when the loan is not paid, "realizing the security" is only possible by making the debtor a slave; and as this is very painful, the creditor who makes much use of it is hated. Even when the land can be pledged, peasant proprietors never think that it ought really to be taken if the debt for which it is pledged is not paid; they think that the land is still theirs, no matter how much has been lent them upon it, or how much they have neglected to pay. But odious as the "usurer" thus becomes, he is most useful really, and the beginner of the movement which creates the "great commerce."

Another condition which precedes the free transfer of labor — the first prerequisite of the free transfer of capital — is slavery; and within its limits this is free enough, — indeed, more free than anything

else similar, for you have not to consult the laborer at all, as in all other organizations you must. The capitalist buys the slave, and sets him to do not what the slave likes, but what he himself likes. I can imagine that a theorist would say beforehand that this was the best way of getting things done, though not for the happiness of the doer,* — it makes the "working group" into an army where the general is absolute, and desertion penal; but so subtle is the nature of things, that actual trial shows this structure of society not to be industrially superior to all others, but to be very ineffectual indeed, and industrially inferior to most of them. The slave will not work except he is made, and therefore he does little; he is none the better, or little the better, if he does his work well than if he does it ill, and therefore he rarely cares to do it very well. On a small scale, and under careful supervision, a few slaves carefully trained may be made to do very good work; but on any large scale it is impossible, — a gang of slaves can do nothing but what is most simple and easy, and most capable of being looked after. The Southern States of America, for some years before their rebellion, were engaged in trying, on the greatest scale and [with] the most ample means the world has ever seen, the experiment how far slavery would go; and the result was short, — they never could "make brute force go beyond brute work."

Next, in order that capital can be transferred, it must exist and be at the disposal of persons who wish to transfer it. This is especially evident as to remunerative capital, which we have seen to be the most transferable of all capital; but the earliest wages-paying commodities — the food and the necessaries which in simple communities the laborer desires —

* This is exactly what Carlyle does say, *passim;* and that it is for the *welfare* of the doer even if not for his happiness. See especially "Life of Sterling," Part ii., Chap. ii., and "Latter Day Pamphlets," No. 1 ("The Present Time"). — Ed.

are accumulated by persons who want them for their own use, and who will not part with them. The "untransferable" laborer — the laborer confined to a single occupation in a primitive society — saves certain things for himself, and needs them for himself, but he has no extra stock. He has no use, indeed, for it: in a society where there is no transferable labor or need to hire, there is no motive, or almost none, for an accumulation of wages-paying capital which is to buy labor. The idea of it, simple as it seems to us, is one of a much later age, like that in which labor seeking to be hired is the commonest of things, and therefore the commodities needed for hiring it are among the commonest too. The means of buying and the thing bought inevitably in such a case as this grow together.

As to the other kind of capital, — that which aids labor, the co-operative kind, — the scientific study of savage tribes, which is so peculiar a feature of the present world, has brought out its scantiness — I might say its meanness — almost more distinctly than it has brought out anything else. Sir John Lubbock, one of our greatest instructors on this matter, tells us the implements of the Australians

"are very simple. They have no knowledge of pottery, and carry water in a small vessel made of bark. They are quite ignorant of warm water, which strikes them with great amazement. Some of them carry 'a small bag about the size of a moderate cabbage net, which is made by laying threads loop within loop, somewhat in the manner of knitting used by our ladies to make purses. This bag the man carries loose upon his back by a small string, which passes over his head; it generally contains a lump or two of paint and resin, some fish-hooks and lines, a shell or two out of which their hooks are made, a few points of darts, and their usual ornaments, which includes the whole worldly treasure of the richest man among them.'"*

All travelers say that rude nations have no *stock* of anything, — no materials lying ready to be worked up, no idle tools waiting to be used; the whole is

* "Prehistoric Times," page 349 (Chap. xi.).

a "hand-to-mouth" world: and this is but another way of saying that in such societies there is no capital of this kind to be transferred. We said just now that what we meant by "transfer" in such a case was a change in the sort of stock, — the kind of materials, the kind of machines, the kind of living things to be used fastest and worn out quickest; but in these poverty-stricken early societies there is substantially no such stock at all. Every petty thing which there exists is already being used for all its petty purposes, and cannot be worked more quickly than it already is, or be worn out more rapidly than it is being worn out.

Next, this capital must be concentrated in "trades," else it cannot be transferred from trade to trade for the sake of profit; and it must be worked by a single capitalist or little group of capitalists, as the case may be, else the trade will not yield profit: and this, as has been explained, is not a universal feature of all times, but a special characteristic of somewhat advanced eras. And there must be the knowledge capable of employing that capital, — a knowledge which altogether differs in different trades. Nowadays the amount of the difference is a little disguised from us because we see people with "capital" in various pursuits, — that is, who are traders in each and all of them; but such persons could not do this unless they were assisted by more specialized persons. The same principle governs political administration. Sir George Lewis, one of the most capable judges of it in our time, has observed:

"The permanent officers of a department are the depositaries of its official tradition; they are generally referred to by the political head of the office for information on questions of official practice, and knowledge of this sort acquired in one department would be useless in another. If, for example, the chief clerk of the criminal department of the Home Office were to be transferred to the Foreign Office, or to the Admiralty, the special experience which he has acquired at the Home Office, and which is in daily requisition for the guidance of the Home Secretary, would be utterly

valueless to the Foreign Secretary, or to the First Lord of the Admiralty. . . . Where a general superintendence is required, and assistance can be obtained from subordinates, and where the chief qualifications are judgment, sagacity, and enlightened political opinions, such a change of offices is possible; but as you descend lower in the official scale, the specialty of functions increases, — the duties must be performed in person, with little or no assistance, and there is consequently a necessity for special knowledge and experience. Hence the same person may be successively at the head of the Home Office, the Foreign Office, the Colonial Office, and the Admiralty; he may be successively President of the Board of Trade, and Chancellor of the Exchequer; but to transfer an experienced clerk from one office to another would be like transferring a skillful naval officer to the army, or appointing a military engineer officer to command a ship of war."*

And just so in mercantile business, — there are certain general principles which are common to all kinds of it, and a person can be of considerable use in more than one kind if he understands these principles, and has the proper sort of mind; but the appearance of this common element is in commerce, as in politics, a sign of magnitude, and primitive commerce is all petty. In early tribes there is nothing but the special man, — the clothier, the mason, the weapon maker. Each craft tried to be, and very much was, a mystery except to those who carried it on; the knowledge required for each was possessed by few, kept secret by those few, and nothing else was of use but this monopolized and often inherited acquirement, — there was no "general" business knowledge. The idea of a general art of money-making is very modern; almost everything ancient about it is individual and particular. Distance helped much in this kind of specialty: to the great fair of Stourbridge, in the South of England, there came, we are told, beside foreign products,

"the wool-packs, which then formed the riches of England, and were the envy of outer nations. The Cornish tin-mine sent its produce, stamped with the sign of the rich earl who bought the

* See also Vol. iii., pages 230, 231.

throne of the German empire, or of the warlike prince who had won his spurs at Crecy and captured the French king at Poictiers. Thither came also salt from the springs of Worcestershire, as well as that which had been gathered under the summer sun from the salterns of the eastern coasts. Here too might be found lead from the mines of Derbyshire, and iron, either raw or manufactured, from the Sussex forges." *

In an age when locomotion was tedious and costly, the mere distance of the separate seats of industry tended to make separate monopolies of them. Other difficulties of transferring capital were aggravated by the rarity and the localization of the knowledge necessary for carrying it on.

Next, as we have seen, for the attraction of capital from trade to trade, there must be a money in which to calculate such profits, and a good money too. Many media of interchange which have been widely used in the world, and which are quite good enough for many purposes, are quite unfit for this. Cattle, for instance, which were certainly one of the first used kinds of money, and which have been said to have been that most used, because what we call the "primitive ages" lasted so long, are quite inadequate. They are good enough for present bargains, but not for the forward and backward looking calculations of profit and loss; the notation is not distinct enough for accuracy. One cow is not exactly like another: a price list saying that so much raw cotton was worth 20 cows, and so much cotton worth 30 cows, would not tell much for the purpose; you could not be sure what cows you would have to give or you would get, — there might be a "loss by exchange" which would annihilate profit. Until you get good coined money, calculations of profit and loss that could guide capital are impossible.

Next, there must be the means of shifting "money," which we analyzed: the loan fund, the

* Thorold Rogers, "History of Prices," Vol. i., pp. 141, 142; rewritten in his "Work and Wages," page 151.

speculative fund, and the choice of employment by young capitalists, or some of them. The loan fund on a small scale is, as we have seen, a very early institution; it begins in the primitive village almost as soon as any kind of trade begins at all, and a perception of its enormous value is one of the earliest pieces of true economical speculation. "In the Athenian laws," says Demosthenes, "are many well-devised securities for the protection of the creditor; for commerce proceeds not from the borrowers, but from the lenders, without whom no vessel, no navigator, no traveler could depart from port."* Even in these days we could hardly put the value of discounts and trade loans higher. But though the loan fund begins so early in civilization, and is prized so soon, it grows very slowly; the full development — modern banking such as we are familiar with in England — stops where the English language ceases to be spoken. The peculiarity of that system is, that it utilizes all the petty cash of private persons down nearly to the end of the middle class: this is lodged with bankers on running account, and though incessantly changing in distribution, the quantity is nearly fixed on the whole, for most of what one person pays out, others almost directly pay in: and therefore it is so much added to the loan fund which bankers have to use, — though as credit is always precarious, they can of course only use it with caution. Besides this, English bankers have most of the permanent savings of little persons deposited with them, and so have an unexampled power of ready lending. But ages of diffused confidence are necessary to establish such a system, and peculiar circumstances in the banking history of England, and of Scotland still more, have favored it; our insular position, exempting us from war, and enabling our free institutions to develop both quietly and effectually, is at the very root of it. But here until within a hundred years

* Oration against Phormio, at the close.

there was no such concentration of minute moneys, no such increment to the loan fund, and abroad there is nothing equal to it now; taking history as a whole, it is a rare and special phenomenon. Mostly the loan fund of a country consists of such parts of its moneyed savings as those who have saved them are able to lend for themselves. As countries advance, banking slowly begins; and some persons who are believed to have much are intrusted with the money of others, and become a sort of middlemen to put it out: but almost everywhere the loan fund is very small to our English notions. It is a far less efficient instrument for conveying capital from trade to trade everywhere else than here; in very many countries it is only incipient, in some it can hardly be said to exist at all.

The speculative fund, as I have called it, has also but a bounded range of action. The number of persons who have large moneyed savings who are willing to invest them in new things is in England considerable, but in most countries it is small. Such persons fear the unknown; they have a good deal to lose, and they do not wish to lose it. In most communities there is not even the beginning of a settled opinion to tell them which undertaking is likely to be good and which bad. In the industrial history of most countries, the most marked feature is an extreme monotony: enterprises are few; the same things continue for ages to be done in the same way. The data which should guide original minds are few and insufficient. There was not such a thing as a "price list" in any ancient community; no Athenian merchant could, by looking over a file of figures, see which commodities were much lower in their average price, and which therefore might be advantageously bought with money that he could not employ in his usual trade. Even for so simple a speculation as this, according to our present notions, the data did not exist; and for more complex ones

the knowledge was either altogether wanting or confined to a few persons, none of whom might have the idle capital. The speculative fund does not become a force of first-rate magnitude till we have in the same community a great accumulation of spare capital and a wide diffusion of sound trade knowledge; and then it does.

The free choice by young men of the mode in which they will invest the capital which they possess is also in the early times of trade much hindered and cramped, and it only gains anything near the effective influence which it now has with us in quite late times. For a long period of industrial history special associations called "guilds" prohibited it; these kept each trade apart, and prevented capital from going from one to the other. They even kept the trade of city A quite apart from the same trade in city B; they would not let capital or labor flow from one to the other. These restrictive hedges grew up naturally, and there was no great movement to throw them down; they strengthened what was already strong, and that which was weak made no protest. The general ignorance of trade matters in such communities made it seem quite reasonable to keep each trade to those who understood it; other people going into it would, it was imagined, only do it ill, lose their money, and hurt those who did it well by a pernicious competition. We now know that this is a great error; that such guilds did far more harm than good, that only experiment can show where capital will answer in trade, that it is from the outsider that the best improvements commonly come: but these things, which are now commonplaces after experience, were paradoxes before it. The first deduction of the uninstructed mind was and is the other way; nor is it dispelled by mere argument, — civilization must increase, trade ideas must grow and spread, and idle capital waiting to change must accumulate; till these things have happened, the free

choice by a young man how he will invest his capital is not the common rule, but the rare exception; it is not what mostly happens though it may be resisted, but what happens only where it is unusually helped. Even where there is no formal guild, the circumstances which have elsewhere created so many create an informal monopoly, mostly much stronger than any force which strives to infringe it.

None, therefore, of the three instruments which now convey capital from employment to employment can in early times be relied on for doing so, even when that capital exists, and when some labor at least is available to be employed by it: neither the loan fund nor the speculative fund nor the free choice of a trade by young men is then a commonly predominant power; nor do the whole three taken together commonly come to much in comparison with the forces opposed to them.

And even if their intrinsic strength had been far greater than it was, it would often have been successfully impeded by the want of a final condition to the free transfer of capital, of which I have not spoken yet; this is a political condition. We have seen that for the free transfer of labor from employment to employment, a strong government is necessary. The rules regulating the inheritance of trades and the fixed separations of labor were really contrivances to obtain some part of the results of the division of labor, when for want of an effectual government, punishing quarrels and preserving life, free competition and movement in labor were impossible; and this same effectual government is equally necessary, as need not be explained, for the free migration of money. That migration needs peace and order quite as obviously as the migration of labor; and those who understand the delicacy of the process will need no proof of it. But though a strong government is required, something more is wanted too: for the movement of capital we need a *fair*

government. If capital is to be tempted from trade to trade by the prospect of high profits, it must be allowed to keep those profits when they have been made; but the primitive notion of taxation is, that when a government sees much money it should take some of it, and that if it sees more money it should take more of it. Adam Smith laid down as a fundamental canon that taxes ought to be levied at the time when, and in the manner in which, it is most easy for the tax-payer to pay them; but the primitive rule is, to take them when and how it is most easy to find and seize them. Under governments with that rule, persons who are doing well shrink from showing that they are doing well; those who are making money refuse to enjoy themselves, and will show none of the natural signs of that money, lest the tax-gatherer should appear and should take as much as he likes of it. A socialist speaker once spoke of a "*healthy* habit of confiscation," and that habit has been much diffused over the world; wherever it exists it is sure exceedingly to impede the movements of capital, and where it abounds, to prevent them.

These reasonings give us a conception of a "pre-economic" era, when the fundamental postulates of political economy, of which we have spoken, were not realized, and show us that the beginnings of all wealth were made in that era. Primitive capital accumulated in the hands of men who could neither move it nor themselves; who really never thought of doing either; to whom either would often have seemed monstrous if they could have thought of it, and in whose case either was still more often prevented by insuperable difficulties. And this should warn us not to trust the historical retrospect of economists, merely because we see and know that their reasonings on the events and causes of the present world are right: early times had different events and different causes. Reasoners like economists — and

there are many others like them — are apt to modify the famous saying of Plunket: they turn history not into an old almanac, but into a new one; they make what happens now to have happened always, according to the same course of time.

And these reasonings also enable us to explain what is so common in all writing concerning those early and pre-economic times. One of the commonest phenomena of primitive trade is "fixed" prices; and the natural inquiry of every one who is trained in our political economy is, How could these prices be maintained? They seem impossible according to the teaching which he has received, and yet they were maintained for ages; they lasted longer than many things nowadays which we do not reckon short-lived. One explanation is, that they were maintained by custom; but this fails at the crisis, for the question is, How could the custom be maintained? The unchanging price could not always be right under changing circumstances. Why did not capital and labor flow into the trades which at the time had more than their "natural" price, desert those which had less, and so disturb the first with a plethora and the second with a scarcity? The answer, we now see, is, that what we have been used to call "natural" is not the first but the second nature of men; that there were ages when capital and labor could not migrate, when trade was very much one of monopoly against monopoly. And in such a society, fixing a price is a primitive way of doing what in after ages we do as far as we can; it is a mode of regulating the monopoly, — of preventing the incessant dissensions which in all ages arise about what is a just price and what is not, when there is no competition to settle that price. The way in which "custom" settles prices, — how it gradually arrives at what is right and proper, or at least at what is endurable, — one cannot well say; probably many incipient customary prices break down before the one

which suits and lasts is stumbled upon. But defects of this rule-of-thumb method are no reproach to primitive times; when we try to regulate monopolies ourselves we have arrived at nothing better. The fares of railways — the fixed prices at which these great monopolies carry passengers — are as accidental, as much the rough results of inconclusive experiments, as any prices can be.

And this long analysis proves, so plainly that it would be tedious to show it again, that the free movement of capital from employment to employment within a nation, and the consequent strong tendency to an equality of profits there, are ideals daily becoming truer as competition increases and capital grows; that all the hindrances are gradually diminishing, all the incentives enhancing, and all the instruments becoming keener, quicker, and more powerful.

But it is most important to observe that this ideal of English political economy is not, like most of its ideals, an ultimate one. In fact, the "great commerce" has already gone beyond it; we can already distinctly foresee a time when that commerce will have merged it in something larger. English political economy, as we know, says that capital fluctuates from trade to trade within a nation, and it adds that capital will not as a rule migrate beyond that nation. "Feelings," says Ricardo, "which I should be sorry to see weakened, induce most men of property to be satisfied with a low rate of profits in their own country, rather than seek a more advantageous employment for their wealth in foreign nations;"* but these feelings are being weakened every day, — a class of cosmopolitan capitalists has grown up which scarcely feels them at all. When Ricardo wrote, trade of the modern magnitude was new; long wars had separated most nations from most others, and especially had isolated England in

* "Principles of Political Economy," Chap. vii.

habit and in feeling. Ricardo framed, and others have continued, a theory of foreign trade in which each nation is bounded by a ring fence, through which capital cannot pass in or out; but the present state of things is far less simple, and much of that theory must be remodeled. The truth is, that the three great instruments for transferring capital within a nation, whose operation we have analyzed, have begun to operate on the largest scale between nations. The "loan fund," the first and most powerful of these, does so most strikingly: whenever the English money market is bare of cash, it can at once obtain it by raising the rate of interest, — that is to say, it can borrow money to the extent of millions at any moment to meet its occasions, or what is the same thing, can call in loans of its own. Other nations can do so too, each in proportion to its credit and its wealth; though none so quickly as England, on account of our superiority in these things. A cosmopolitan loan fund exists, which runs everywhere as it is wanted and as the rate of interest tempts it.

A new commodity, one of the greatest growths of recent times, is used to aid these operations. The "securities" of all well-known countries — their national debts, their railway shares, and so on (a kind of properties peculiar to the last two centuries, and increasing now most rapidly) — are dealt in through Europe on every Stock Exchange. If the rate of interest rises in any one country, the price of such securities falls; foreign countries come in and buy them; they are sent abroad, and their purchase money comes here. Such interest-bearing documents are a sort of national "notes of hand," which a country puts out when it is poor and buys back when it is rich.

The mode in which the indemnity from France to Germany was paid is the most striking instance of this which ever occurred in the world. The sum of £200,000,000 was the largest ever paid by one set of

persons to another, upon a single contract, since the system of payments began. Without a great lending apparatus such an operation could not have been effected ; the resources of one nation, as nations now are, would not have been equal to it : in fact, it was the international loan fund which did the business.

"We may say," M. Say states in his official report, "that all the great banking-houses of Europe have concurred in this operation ; and it is sufficient to show the extent and the magnitude of it to say that the number of houses which signed or concurred in the arrangement was fifty-five, and that many of them represented syndicates of bankers, so that the actual number concerned was far more considerable." "The concentration," he adds, "of the effects of all the banks of Europe produced results of an unhoped-for magnitude. All other business of a similar nature was almost suspended for a time, while the capital of all the private banks and of all their friends co-operated in the success of the French loans, and in the transmission of the money lent from country to country. This was a new fact in the economical history of Europe, and we should attach peculiar importance to it."

The magnitude of it as a single transaction was indeed very new, but it is only a magnificent instance of what incessantly happens ; and the commonness of similar small transactions, and the amount of them when added together, are even more remarkable and even more important than the size of this one ; and similar operations of the international "loan fund" are going on constantly, though on a far less scale.

We must not, however, fancy that this puts all countries on a level as far as capital is concerned, because it can be attracted from one to another ; on the contrary, there will always tend to be a fixed difference between two kinds of countries. The old country, where capital accumulates, will always on an average have it cheaper than the new country, which has saved little and can employ any quantity. The Americans in the Mississippi Valley are naturally a borrowing community, and the English at home are naturally lenders ; and the rate of interest in the lending country will of course be less than that in

the borrowing country. We see approaches — distant approaches even yet, but still distinct approaches — to a time at which all civilized and industrial countries will be able to obtain a proportionate share of the international loan fund, and will differ only in the rate they have to pay for it.

The "speculative fund" is also becoming common to all countries; and it is the English who have taken the lead, because they have more money, more practical adaptation to circumstances, and more industrial courage than other nations. Some nations, no doubt, have as much or more of one of these singly; but none have as much of the efficiency which is the combined result of all three. The way in which Continental railways — the early ones especially, when the idea was novel — were made by English contractors is an example of this. When Mr. Brassey, the greatest of them, was making the line from Turin to Novara, for the Italian government, Count Cavour sent one morning for his agent and said, "We are in a difficulty: the public have subscribed for very few shares, but I am determined to carry out the line; and I want to know if Mr. Brassey will take half the deficiency if the Italian government will take the other half." Mr. Brassey did so, and thus the railway was made. This is the international speculative fund in action, and the world is filled with its triumphs.

So large, so daring, and indeed often so reckless is this speculative fund, that some persons have imagined that there was nothing which would seem absurd to it. A very little while ago, a scheme — a fraudulent scheme, no doubt — was gravely brought out, for a ship railway over the Isthmus of Panama; the ships were to be lifted upon the line on one side, and lifted off and returned to the ocean on the other: but even the "speculative fund" would not stand that, and the scheme collapsed.* But the caricature

* The scheme was perfectly *bona fide;* and I suspect Bagehot's sneer will read curiously before many years. — Ed.

shows the reality; we may use it to remind ourselves how mobile this sort of money is, and how it runs from country to country like beads of quicksilver.

Young men also now transfer their capital from country to country with a rapidity formerly unknown. In Europe perhaps the Germans are most eminent in so doing: their better school education, their better trained habits of learning modern languages, and their readiness to bear the many privations of a residence among foreigners, have gained them a prominence certainly over the English and the French, perhaps above all other nations. But taking the world as a whole, the English have a vast superiority: they have more capital to transfer, and their language is the language of the great commerce everywhere, and tends to become so more and more. More transactions of the "cosmopolitan speculative fund" are arranged in English, probably, than in all the other languages of the world put together; not only because of the wealth and influence of mere England, though that is not small, but because of the wealth and influence of the other states which speak that language also, — the United States, our colonies, and British India, which uses it mostly for its largest trade. The number of English commercial houses all over the world is immense, and of American very many; and yearly a vast number of young Englishmen are sent out to join them. The pay is high, the prospect good; and insular as we are thought to be (and in some respects we are so most mischievously), the emigration of young men with English capital, and to manage English capital, is one of the great instruments of world-wide trade and one of the binding forces of the future.

In this way the same instruments which diffused capital through a nation are gradually diffusing it among nations, and the effect of this will be in the end much to simplify the problems of international trade; but for the present, as is commonly the case

with incipient causes whose effect is incomplete, it complicates all it touches. We still have to consider, after the manner Ricardo began, international trade as one between two or more limits which do not interchange their compound capitals, and then to consider how much the conclusions so drawn are modified by new circumstances and new causes. And as even when conceived in Ricardo's comparatively simple manner, international trade, as Mr. Mill justly said and as the readers of his discussion on it well know, is an excessively difficult subject of inquiry, we may expect to find many parts of it very hard indeed to reduce to anything like simplicity when new incumbrances are added. The popular discussion of the subject tends to conceal its difficulties, and indeed is mostly conducted by those who do not see them; nothing is commoner than to see statements on it put forth as axioms which it would take half a book really to prove or disprove: but with the soundness or unsoundness of such arguments I have at present nothing to do. The object of these papers is not to examine the edifice of our English political economy, but to define its basis: nothing but unreality can come of it till we know when and how far its first assertions are true in matter of fact, and when and how far they are not.

THE PRELIMINARIES
OF
POLITICAL ECONOMY.*

I.

Adam Smith began the "Wealth of Nations" about 1773, and finished it in 1776; and as our modern political economy really begins from that time, we may fairly say that it is now a hundred years old. In that century, especially in England, its career has been most remarkable. No form of philosophical speculation (some theologies excepted, which are not comparable) has ever had half or a thousandth part of the influence upon life and practice; no abstract doctrine was ever half as much quoted or half as much acted on. The whole legislation of England as to trade has been changed by the philosophy of trade, and the life of almost every one in England is in consequence different and better. Other countries, it is true, have not equally followed this teaching, but they have continually if not equally discussed it; the highest class of cultivated intellects is in every civilized country more or less affected by it. When a little while ago M. Thiers began to talk and act in thorough opposition to the whole science, a shiver of wonder ran through Europe: it seemed an anachronism to

* Written in 1876 or earlier. It will be obvious that some of the leading ideas of the previous essays are repeated in this. There is, however, so much that is fresh in it, and so much danger of bungling in any attempt to disentangle the fresh matter from what was embodied in the two previous essays, that it has been thought better to run some little risk of repetition rather than to attempt any separation of the old and new by any other hand than the author's. — R. H. H.

find so able a mind in the pre-economic period, and a strange survival of extinct error to hear him expounding the good of all which political economy showed to be bad and the evil of all which political economy proved to be good. No kind of political teaching has ever won half as many triumphs, or produced half the effects.

But nevertheless, the reputation of political economy is not altogether satisfactory to the minds of those who most value and prize it; there is not quite the same interest felt for it, or quite the same confidence reposed in it, which there was formerly. A small knot of persons deny its value; a good many people, though sure they are wrong, are puzzled by them and do not see how to answer them. Many young men, even studious men, especially those educated abroad, have not studied its best writers, and have but vague views about it. Though victorious, it wants part of the prestige of victory; though rich in results, its credit is not quite as good as on that account it ought to be.

The truth is, that the story of political economy, if I may so call it, is a curious one in itself; the science is to some extent a new sort of one in the world, and has come to be what it is in a rather strange way. That story could only be fully explained by an exposition of all the science, and an account of all who contributed to it. But I think the main and most valuable part of the truth may be set before those who will read a short description of the science as it now stands, and a rough account of the labors of four great men,* who more than any others have made the science what it is and placed it where it is. The knowledge so given will after all be most imperfect.

* The essay on J. S. Mill was not written, and that on Adam Smith is incomplete. — R. H. H. The latter name must be a slip for "Ricardo": the essay on Adam Smith is quite full, while that on Ricardo is a mere scrap, without a word on his special economic doctrines or his relation to the science as it stands. — Ed.

II.

Political economy in its complete form, and as we now have it, is an abstract science, just as statics or dynamics are deductive sciences; and in consequence it deals with an unreal and imaginary subject. Just as statics and dynamics — the sciences of theoretical mechanics — deal with perfectly rigid bodies, which nothing will bend or strain; with perfectly elastic planes, from which the rebound is equal to the impact; with a world destitute of friction; with physical materials, in short, which no one ever expects to find in reality, — so political economy deals with an immaterial subject, which in the existing world cannot be found either. Political economy deals not with the entire real man as we know him in fact, but with a simpler, imaginary man, — a man answering to a pure definition, from which all impairing and conflicting elements have been fined away. The abstract man of this science is engrossed with one desire only, — the desire of possessing wealth; not of course that there ever was a being who always acted as that desire would dictate, any more than any one thinks there are in nature a world without friction or entirely elastic planes, but because it is found convenient to isolate the effects of this force from all others. The effect of the abstract hypothesis made on the necessary basis of statics and dynamics is, to enable us to see the effect of the single agent "pressure," in a simple way and free from the repressing and obscuring conditions which exist in actual nature; and in the same way the use of the primitive assumptions of political economy is, to show how the greatest of industrial desires — the desire to obtain wealth — would operate, if we consider it as operating as far as we possibly can by itself. The maxim of science is simply that of common-sense — simple cases first; begin with seeing how the main force acts when there is as little as possible to impede

it, and when you thoroughly comprehend that, add to it in succession the separate effects of each of the incumbering and interfering agencies.

If such a simplification is necessary in physical science, where the forces are obvious and few, it must much more be necessary in dealing with the science of society, where the forces are in comparison very various and difficult to perceive. In this very science of political economy, the first writers endeavored to deal in a single science with all the causes which produced or impaired wealth, — which, as they would have said, "made nations rich or poor;" and this was the most natural way of beginning, — almost all science seems to have begun similarly. In each case there was some large palpable fact to be explained, some great pressing problem to be solved; and so here, if you look over the nations of the world, you see at once that one of the greatest contrasts between them is that of comparative wealth or comparative poverty. The palpable fact at the beginning of political economy is, that the Dutch are rich and others (the Tyrolese, suppose) poor, that England is a very rich country and Ireland a very poor country: how then was this difference to be accounted for, and the practical problem — money being an admitted good — to be solved, How far can we make the poor nations rich, and how are we to begin so to do? But considered in this simple and practical way, the science of political economy becomes useless, because of its immense extent: the whole of a man's nature and the whole of his circumstances must be reckoned up and reasoned upon before you can explain his comparative wealth or poverty. To explain the difference of industrial conditions between the Tyrol and Holland, you will have first to state all the points of difference in religion, in morality, and in inherited character between a Dutchman and a Tyrolese, then state the diversities of their physical condition, and work out as best you can the effects

of all the contrasts. And still further, if you try to give a universal reason why nations are poor and why nations are rich, you will not be able to arrive at any useful answer. Some will be poor because they have a bad government; some because they are cooped up on a poor soil; some because they have a religion which disinclines them to make money; some because they have ancient rules, which helped them to make a beginning but now retard them; some because they have never been able to make that beginning: and many other cases might be given. The problem taken up in that form is indeterminate: why nations are rich or poor depends on the whole intrinsic nature and all the outward circumstances of such nations. There is no simpler formula to be discovered, and a science which attempted to find one would of necessity have to deal with the whole of physical science; it would be an account of all "men" and all the earth.

It is on account of its abstract character that political economy is often and justly described as a science of "tendencies" only; that is, the object of it is, to work out and ascertain the result of certain great forces, as if these alone operated, and as if nothing else had any effect in the matter. But as in matter of fact many other forces have an effect, the computed results of the larger isolated forces will never exactly happen: they will only, as it is said, tend more or less to happen; that is, they happen more and more nearly in proportion as the resisting and perturbing causes in each case happen to be less and less.

The very refined nature of the modern science of political economy has naturally led to many mistakes about it. The mere idea of such a science has evidently never crossed the minds of many able writers, and persons who have given but slight consideration to the matter are much puzzled. Analogous sciences on physical subjects are, as has been

said, easy to find; but illustrations from them do not tell much where effectual description of political economy is most wanted. A science occupied with human things, and professedly with a part of human things profoundly interesting, awakens a great curiosity among multitudes of little cultivation. They begin to think about it and to read about it; and the better the books they read, the more likely are they to be puzzled by what they find. They know that they are reading words which are constantly used in common life, and about things resembling at least those of that life; but nevertheless, the reasonings and the conclusions do not seem to belong to real life at all. Such persons know nothing about statics or dynamics, and any attempt to explain the nature of political economy by an account of the nature of statics or dynamics is only explaining *obscurum per obscurius*. As might be expected, the worst offenders are the uncultured moralists: they see all manner of reasonings framed, and of conclusions drawn, apparently about subjects with which morality itself is concerned deeply, — about (say) industry and wealth, population and poverty, — and they never dream that there is anything peculiar about these conclusions. They apply the "rules of morality to them at once"; they ask, "Is argument B true of good persons? Would not conclusion C augment wickedness?" whereas in fact the economical writers under consideration did not mean (and rightly did not mean) to deal with ethics at all. They only evolved a hypothesis; they did not intend that their arguments should be thought to be taken from real life, or that their conclusions should be roughly and as they stood applied to real life. They considered not the whole of actual human nature, but only a part of it; they dealt not with man the moral being, but with man the money-making animal.

Naturally, too, the cultivators of the abstract science itself (even those who fully understood its peculiar

nature) did not always in practice remember the remoteness to practice of that nature. On the contrary, they rushed forth into the world with hasty recommendations to instant action; whereas the very justification of their reasonings, and the very ground of their axioms, was the necessity of beginning the investigation of the subject in a simple theory, and far away from the complexities of practice and action. But so much are the practical impulses of man stronger than his theoretical tastes, that the cultivators of an abstract science are always in great danger of forgetting its abstract nature; they rush and act on it at once. In the abstract physical sciences there is an effectual penalty, — a person who acted on abstract dynamics would soon break his head; but in mental and physical sciences, unhappily, there are no instant tests of failure, — whatever happens, a man can always argue that he was right: and thus an abstract science of human things is more delicate to handle, and more likely to be misused, than a similar science of external nature.

A sort of uncertainty likewise seems, even in the better informed minds, to creep over the subject. If it is so remote from practice, they say, how can you test it, and how can you tell that it is true? But this is exactly so also in the corresponding physical sciences. One of the shrewdest observers of intellectual matters of the generation, the late Sir G. C. Lewis, used to say: —

"My experience in this office" (he was then Secretary of State for War) "has convinced me that when you come to practice, physics are just as uncertain as metaphysics. The abstract theory of physics is unquestionably much more complete: but if you want to deal with an instance in life, you will always find that there is a 'tension,' or a 'friction,' or some other cause, which is not accurately measured and does not figure in the abstract theory; and this is the reason why, on all such questions, scientific evidence is so conflicting. You can always obtain an eminent engineer on any side to set against an eminent engineer on the other

side; because the scientific and certain part of the subject is not the whole, and there still remains an imperfectly explored *residuum* on which there may be different opinions."*

All this is as true of political economy as of any physical science; its deductions may be incontrovertible, and its results precisely true, whenever its assumptions are true; but these results will be very imperfect guides wherever those assumptions are impaired by contradictory matter.

On the other side, however, it should also be said that "abstract" political economy is not by any means the unnatural thing which, from the account of it on paper and the description of its difficulties, it would seem to be. Many people on the matter have "talked prose all their lives without knowing it"; many people have given admirable arguments on political economy, and have been more or less precisely aware of the difference of their assumptions from those of the real world, though they have never studied the specially abstract science, and could have given no sufficient delineation of it. The notion of investigating how much money persons would make who simply wished to make it, and how they would best do so, is a very simple idea. The desire for wealth — using "wealth" in the largest sense, so as to include not only the means of luxury, but the means of subsistence — is so preponderant in very many minds that it is very easy, if necessary, to regard it as the sole object. As far as people are what we now always call "men of business," money, the thing they look for and the thing they want, is their sole object; and in that sense of the phrase, political economy may be fairly called the science of "business."

On that account, in some very large scenes of our present English life, political economy is exactly true; the primary assumption on which it rests is precisely realized. On the Stock Exchange everybody does act

* Repeated in Vol. iii., pages 244, 245

from a love of money; men come there to make it, and they try to make as much of it as they can. Of Lombard Street the same may be said: the pecuniary phenomena of Lombard Street may be investigated with quite sufficient accuracy on the assumption that bankers come there only to make money, and when there, make as much of it as they can. All markets are scenes nearly similar: so long as they are at the market, all dealers try to make the best bargain they can. As the principal nations of the world at present are nations of business, — commercial nations, — and as the mass of men in such nations are mainly occupied in business, it follows that with respect to those nations a simple analysis of the unchecked consequences of the "business motive" will be a near approximation to a large part of their life; though it will not be a perfect account of their complete career, for there is very much also in every nation besides business and besides money, — but it will be a useful hint to a predominant characteristic of that career. Having investigated the effects of this principal motive, we may when we please, and as far as it is necessary, investigate the effects of the almost infinite number of the secondary and interfering motives.

As, too, it is at present necessary for all nations to be rich in order to be influential in the world, it follows further that an account of the commercial motive of action, taken by itself, is, as the world now stands, an analysis of the results of a principal ingredient in the days that are gone by, when poor barbarians, if warlike, were more powerful than rich civilized people. The times are gone by when civilization enervated energy, or when wealth impeded valor. At present, courage without money is courage without guns; and courage without guns is useless. Political economy traces in an abstract way the effects of the desire to be rich; and nations must nowadays abound in that passion if they are to have much power or much respect in the world.

On the other hand, no intellectual attempt can be more absurd than the attempt to apply the conclusions of our political economy to the lives of nations at a non-commercial stage of their existence. A great military nation based on slavery, like the Romans; a nation bound by fixed customs, like so many Oriental nations; tribes in a state of barbarism, — are not guided principally by the commercial spirit. The money-getting element is a most subordinate one in their minds; its effects are very subordinate ones in their lives. As the commercial element is all but necessary to considerable combinations of men, that element will almost always have effects, and usually important effects, in the destiny of these combinations; but only in communities where the commercial element is the greatest element will these effects be the greatest. In so far as nations are occupied in "buying and selling," in so far will political economy, the exclusive theory of men buying and selling, come out right, and be true of them. But it will be good as far as it goes; and though it is not my business to say it, I think it will be the fault of the writer if the curious interest of the facts does not lead many readers to a further study of the subject.

And though what has been explained is the principal difference between the hypothetical science of political economy and the real world, it is by no means the only difference. Just as this science takes an abstract and one-sided view of man, who is one of its subjects, so it also takes an abstract and one-sided view of wealth, which is its other subject. Wealth is infinitely various; as the wants of human nature are almost innumerable, so the kinds of wealth are various. Why men want so many things, is a great subject fit for inquiry; which of them it would be wise for men to want more of, and which of them it would be wise to want less of, are also great subjects equally fit: but with these subjects political

economy does not deal at all; it leaves the first to the metaphysician, who has to explain if he can the origin and the order of human wants; and the second to the moralist, who is to decide to the best of his ability which of these tastes are to be encouraged, and when, — which to be discouraged, and when. The only peculiarity of wealth with which the economist is concerned is its *differentia specifica*, — that which makes its wealth; to do so it must gratify some want of man, or it would not be desirable, or it would not be wealth. But whence that want comes, — whether from a low part of man or from a high, — is to the economist immaterial; whether it is a desirable want for man to gratify he cares as little, so long as that gratification does not hurt man as a wealth-producing machine. He regards a pot of beer and a picture, a book of religion and a pack of cards, as all equally "wealth," and therefore, for his purpose, equally worthy of regard. The only division of wealth in his mind is, if I may use the words, the division between sterile and not sterile. Some things will help men to make new things; some things will induce men to work and make new things: both these classes of things are, in the eyes of the economist, capital or reproductive. On the other hand, other things have no similar reproductive power; if they were taken out of the world, all work would go on with equal efficiency, and as many new things would be produced: and these last are, in the eyes of the economist, unproductive opulence, just as the first were productive capital.

Further, political economy makes not only these assumptions as to the nature of its principal force and as to that of its object, it also makes two as to the physical conditions under which this force acts, and in which this object is supposed to exist. For its own purposes it simplifies, as we have seen, the nature of the actors and the end of the action; we have now to see that it simplifies also the stage.

Political economy assumes that land is "limited in quantity and variable in quality"; and taking the whole of human tastes,* this assumption has almost always been true. There has been in almost all countries a difficulty in obtaining land; there has scarcely ever been a surplus of it. Still, though this assumption accurately coincides with the usual phenomena of most countries, it does not agree with all the phenomena of them all. On the contrary, in all "new" countries, as they are called, land is exceedingly plentiful: there is practically no difficulty in procuring it; in the valley of the Mississippi as much of the best land as any one wants can, without serious impediment, be obtained. No doubt such land is further off from the best markets than most occupied land of a like kind; but in the present state of the arts, such a difference in distance presents no serious difficulty. The construction even of a short railway will open up an entire district, and make its produce as available in the market as that of much land long before cultivated. In new countries it can hardly be said that this assumption of political economy is at all like the truth, — it is rather the opposite of the truth; and accordingly the doctrines of abstract political economy must not be applied to such countries roughly, and without previous re-examination. One of the primitive assumptions not being true, we must be careful to reinvestigate and see whether any particular deduction which we wish to use, is or is not impaired, — is or is not in consequence untrue.

At first sight it would seem that this limitation of abstract political economy would exclude it from much of the real world. New countries, one would imagine, would be among the most common of countries; the human race has always been wandering, and must have been always reaching new countries: but in truth this limitation scarcely makes any new

* Query, "states"? — Ed.

exclusion. The nature of the "man" who first occupied new countries did not "conform" to the standard of economical man; the being of reality was not the being of the hypothesis. The first men, all researches justify us in assuming, nearly approached in nature to the present savage man. They had not probably as many curious customs or so many debasing superstitions; they had not so many ingrained vices: but they had as little intellectual development, and as little knowledge of material things; they were ignorant of the "calendar"; they could with difficulty count more than five; they could just make a few weapons of war; they could just construct some sort of shed that would serve for a dwelling: but they could not make any of the articles which we now call "wealth," and they would not have appreciated such things. The desire, so strong in civilized man, for wealth, has been excited in him by the experience of ages, and has been transmitted to him by inheritance. If you take a present savage, even of a high type, he will find the life of cities, the life of wealth *par excellence*, scarcely tolerable. There is a well-known story of one savage, who, after living some forty or fifty years in a cultivated world, in his old age returned to die as a barbarian, saying that "civilization was so much trouble he could bear it no longer." The first occupiers of most countries were not men eager for complex wealth; they cared only for a bare subsistence—and then to kill and eat one another.

Many ages indeed have always intervened between the first settlement of any country and the rise of a strong and independent mercantile element, before the time at which the first assumption of political economy was at all satisfied in it. During that time such countries commenced a kind of civilization, but it was a very different kind of civilization from the predominantly commercial; it was in general ruled by fixed customs, as most of the East is now; it did

not allow its members to choose their own ends and fix their own existence for themselves, — on the contrary, it chose itself those ends and prescribed that existence. And the life so selected gave but little scope to the production of wealth: it was occupied either with an incessant military service, or in peace with an equally incessant but semi-religious ritual; the labor for and the accumulation of the means of physical comfort were very secondary aims in most of the periods described by history, as they still are in by far the greater part of the present world. For ages after their first colonization, there was no such absorbing and self-selecting life of trade as political economy assumes and requires.

Accordingly, in all the old world, — the world as known to the "ancients," — the land has long been occupied, and more or less usefully, more or less fully, by ancient and ineradicable races; in practice they cannot be dispossessed. In all that large part of the world, therefore, land is very scarce; no new-comers can in fact obtain much of it. But of late there have been immense territories — "new worlds," to use the usual word — of which this is not true, but where the very reverse is true: long voyages, impossible to the ancient navigator, have been made possible by modern inventions; and these voyages have discovered large regions inhabited only by men who fade away before the presence of civilized men. In these distant regions man seems to have been a protected, and therefore a feeble animal; he had not to submit to the incessant competition which has in the "old world" hardened his frame and seasoned his mind. The diseases which the European can bear, the stimulants in which he delights, the labor for which he lives, are so many poisons to the Australian or American savage; he dies of one or all of them soon after the coming of the European, and he leaves his land vacant; he has never been able to cultivate the land which he calls his, and now he drops away from it.

As a singular result of this strange history, land of the best quality is now procurable in large quantities and with great ease by civilized man. There are now countries not only called "new" because newly discovered, but new really, because the land in them can now be used but has never been used before.

As a matter of fact, therefore, the primitive assumption of hypothetical political economy, that land is always limited in quantity as well as variable in quality, coincides well enough with the usual facts of the world; but as the modern exception is one of great present importance to economical nations, as a matter of convenience it has become desirable (though I do not think the desirability has been usually recognized) to annex to political economy a full discussion of the nature and the effects of that exception. What has hitherto been the rule, and what has hitherto been the deviation from it, both become clearer when considered side by side.

It may be asked, What is the use of laying down such a rule, if you admit it* and discuss exceptions to it? Why invent a hypothetical hedge, when you know that it does not include all you want, and that therefore you will be unable to keep within it? The answer is, that the rule was not arbitrarily invented by inward fancy, but suggested by outward facts long predominant; the nearest way to the whole truth is by pursuing the clue which the partial truth first gave.

Political economy also assumes, as another axiomatic fact as to land, that land throughout the world is for the most part of such fertility that the labor of a cultivator, if he has but a very moderate degree of knowledge and skill, will produce not only a subsistence for himself but also many other persons. This is so true that it perhaps scarcely needs to be said, but it is of cardinal importance; if it had

*This word destroys the sense, and should be canceled.—Ed.

not been true, the truths of political economy and the lives of men would have been altogether different from what they now are. And there is no *a priori* reason — in physics, at least — why the whole earth should not be as a bit of bleak moor, where agriculturists have nothing over, and can but just raise a bare subsistence for themselves; but for the most part there is a surplus, and this surplus is of course increased day by day, — by the continual improvement in the arts of agriculture more is produced, and therefore there is more over. In old countries the increasing productiveness retards the need of a resort to new soils, and diminishes the evil of it; and in new countries this additional surplus is an extra fund for exportation, and a new means for supplying the wants of those who have stayed at home in the old world.

And lastly, political economy declines to investigate all the causes which determine the rate of increase of man, and assumes an avowedly incomplete and approximate formula as to it. From the very nature of the case, political economy must do this. The causes which regulate the increase of mankind are little less than all the causes, outward and inward, which determine human action: climate, social customs, political government, inherited race nature, and other things beside, affect, as we all know, the rate at which population grows. Political economy would have to discuss half physiology, half the science of government, and half several other sciences too, if it attempted to investigate the real laws which regulate the multiplication of mankind; it has necessarily to make an assumption, to assume as a dictum some approximation to the complex truth, which is at once simple enough to be manageable and true enough to be useful. Political economy therefore assumes that in any particular society, the power of parents to produce children exceeds the power to provide for them in what those parents think sufficient comfort; whence

it comes that either parents must not produce all the children that they can, or that if they do the standard of comfort in the population must deteriorate, and if the multiplication continue and the deterioration augment, that the population must die off. There is no difficulty in showing that this assumption embodies accurately enough the ordinary experience of mankind, as history records it and as present facts evince it: an immense "reserve power" of multiplication is certainly to be found in most countries, which is kept down by one obstacle or other, but which is ready to start forward when that obstacle is removed. No two countries can differ more in every respect important for this purpose than Great Britain and British India; yet both of them seem to prove the same result. At home, the people of Great Britain increase only at the rate of 1.01 per cent. per annum, and double in 58 years; but if you take the very same population to the colonies or the United States, it is believed to increase at a much more rapid rate, and to double itself more rapidly, though the relative increase is not nearly so great as is sometimes assumed when no sufficient account is taken of the continual immigration into those countries. The lesson of Hindostan is still more remarkable. The population of the Peninsula is ordinarily supposed not to have augmented since the time of Alexander; there is conclusive evidence that for centuries preceding the English conquest it augmented very slowly, if at all: but now, under the influence of long peace and long good government, the population is beginning to augment very rapidly. In the North-West Provinces, where the data are the best, it is said to be augmenting almost as rapidly as the population of Great Britain. Here as before there is an immense acceleration of the rate of multiplication, because a repressive force has as before been withdrawn. No one can doubt that the same experiment would have a like result in other cases.

It may be said that out of Europe there is very much unoccupied land, and that even if Europe produced all the people it could, those people might be sent thither; but emigration on such a scale, though imaginable in speculation, is not possible in practice. To create very rapidly new colonies, or to extend very rapidly old ones, requires the migration not only of persons but of capital: you must send thither the means of subsistence if the emigrants are to be subsisted, and the means of employment if they are to be employed. And capital will not go unless you pay it; it must have its regular percentage: and as yet no capital employed in founding colonies —not capital, that is, of a founding company, or of founders as such—has ever paid a farthing. The capital so expended has been a great benefit to the emigrants and to the colony, but it has never paid a dividend; on the contrary, the whole capital has commonly been lost. There are no means by which owners at home can be sure of their interest; nor will very many owners of capital go themselves to the colonies, only because it would much help the poor there if they did so. Capital must be propelled by self-interest; it cannot be enticed by benevolence. The sudden foundation of a colony so huge as to contain all the *possible* children—all those that might be in excess of those which are—is impossible; the bare idea of it is ridiculous.

Nor if such a colony could be founded, would it attain the end desired. Cultivated persons in Europe do not produce all the children they might, because they know that if they did, those children could not lead any such life as they themselves lead. They wish their children to have refined habits, and to live by their talents and their mind as they do themselves; but in a colony this is simply impossible, —rude plenty and rough prosperity are common, but a nice refinement is all but impossible. The life of a lady, as we see it in Europe, is in colonies impossible:

as sufficient servants cannot be obtained, the mother of the family has in person to see to the manual slavery of the housework as well as look after her children, and this leaves her little opportunity for refined culture. The men are a little better off, but not much: the demand for educated labor in the colonies is exceedingly small, — the business of the place is to produce corn or wool, food or raw material; neither skilled labor nor cultured labor are much wanted for that. Almost all our colonies have warned our artisan[s] not to come thither, because there was no room; and as for the legal or other long-trained and costly mental labor of the old world, there is very little opportunity for it. Not only, therefore, is a colony impossible which should be huge enough for all the possible people of the old world, but such a colony, even if possible, would be inadequate: it would only provide for the children of rude people in the manner rude people wish, it would not provide for those of refined people in the least as refined people wish.

The measured use of the multiplying power which is now practiced by all decent people in the existing society of the old world is, therefore, more or less essential to the continuance of such a society. A use of the power without measure would certainly overcrowd such societies with high aims that could not be satisfied, and perhaps also with mouths which could not be fed.

And it is quite consistent with this to believe that such restraint has not at all been uniformly practiced in the world; that it has been rather the rare exception, not the common rule. Such restraint has not been practiced because it has not been wanted. We have been let into the secret of the matter by the experience of India: the number of the people in British India, as we have seen, was stationary for ages, but now they have begun to augment quickly; and we know the reason why.

And it is, too, quite consistent with this doctrine to believe, as has been lately urged with singular force, that we have as yet much to learn as to the theory of population: that the numbers of all nations do not augment alike even under seemingly similar conditions; that there is the same difference in different families; that there are a variety of "laws" — some that can be clearly indicated, others that can be only suspected — which diminish or seem to diminish the multiplying capacity of mankind.

One of these is the increase of intellectual action. Physiologists say, on *a priori* ground, that if you spend nervous force in one direction you will not have as much to spend in another. The ultimate identity of seemingly different forces is one of the most remarkable discoveries of recent science, and there is every reason to think that it applies here; an incessant action of the brain often seems to diminish the multiplying power. It can hardly be an accident that Shakespeare, Lord Bacon, Milton, Newton, and Locke — perhaps our five greatest Englishmen — had only six children between them.* Locke and Newton, it is true, did not marry; but it is not irrational to suspect that the coolness of temperament which kept them single was but another phase of the same fundamental fact. But the doctrine of abstract physiology must be applied with caution. It only says that of any particular total of nervous force, what is expended in one way will not remain to be expended in another; in any given case, to use the well-known phrase, "what is gained in children will be lost in mind:" but all cases are not alike. The nervous power of A may be fifty times that of C, and therefore he may do five times more brain work than C and also have five times his children; and in fact, Mr. Galton finds that English judges — a strongly

*There may be some doubt as to Newton and Shakespeare, but this is the number as far as it can be authenticated. — B.

intellectual race as a whole — have as many children as other people, and there are some other limiting observations which might be made on the subject. Still, on the whole there seems to be a tendency in the absorbing action of intellectual power to have this particular effect, and abstract science teaches that we should expect it.

The same remark, with some limitations, is probably also applicable to women. Hardly any one who observes can doubt that women of much mind and fine nerves, as a rule, seem not so likely to have children, or at least not to have so many children, as others. Here too, as with men, the whole vital force in one case often may be, and often will be, different from that force in another, and therefore particular women may be up to the average, or even be remarkable in both ways; but still, on the whole, the existence of the tendency seems clear. And it is curiously like a similar force at the other end of the social scale: Mr. Wallace, one of the most competent of living observers, says that the increase of the population in savage tribes is much retarded by the exhausting labor of their women; and it will be a curious cycle if, as is likely, in the latest civilization the same preventive check should again become a powerful one.

Another force which may be strongly suspected, if it cannot be quite proved, is the tendency of disheartened races and of dispirited families to die out and disappear. This force would seem to be much the same as that which operates on all wild animals when in confinement: the richest food may be given to such animals, the greatest care taken of them, and their apparent health may seem to be as good as possible, and yet they will not breed. Now, all such animals are dispirited for want of the excitement of a wild life, and this may be the reason of the change in their multiplying power; at any rate, in the case of men, close observers of the dying savage races seem to think that often the mind has something to

do with it. The New-Zealander says that "as the English rat has supplanted the Maori rat, so the English 'man' will supplant the Maori 'man';" he looks on the extinction of his race as a fixed fate, and in consequence his spirits fall, his mind loses some of its tone and his constitution some of its vigor. In civilized life particular families sometimes seem to droop and die away, though it is not possible to set down the cases exactly in figures; this is analogous to what Dr. Maudsley tells us he has observed of anxiety.

All these seem to be traces of new laws which already diminish, and in future times may still more limit, the multiplying power of mankind; but the fullest acknowledgment of them does not contradict the primary assumption made by abstract political economy. It will still remain true, at present, that if all people had as many children as they could, they could not provide for them as they think they ought, —perhaps could not provide for them at all. Nor is it easy to imagine a future time when causes such as these should have so exceedingly diminished the sexual feelings as to make voluntary restraint of them needless; those feelings certainly are incredibly strong now, in comparison with the forces which it is thought will hereafter supplant them: it is easy to believe that the necessity for voluntary restraint should be diminished, but it is not easy even to imagine that this necessity should be extinguished.

In the same way this primary axiom would not be impaired if it could be proved that aristocracies, as such, tend to have fewer children than other classes: aristocracies are so small a fraction of mankind that the particular rate of their increase is not important enough to alter much the rate of increase of mankind, or even of a nation as a whole. But though this tendency of aristocracies has often been imagined, it has never been proved, and indeed it never will be, for it can be easily disproved. The

most obvious and conclusive fact against it is, that the English aristocracy have more children than the average of Englishmen. A common observer of society would indeed expect to find this: he would remember that the peers now differ very little from the rest of the English gentry; that the English gentry are as a rule healthy and not dissipated men; that peers in general are married early; all these characteristics make them likely to have more children than other people, and in fact they have more. The theory that aristocracies of necessity diminish in number fails in this case even ludicrously; for that theory attributes to the persons it selects a deficiency in the very particulars in which they were likely to excel, and do excel.

But though this assumption as to the multiplying power of the people is true of by far the greater part of the world, and of most ages, it is not true of all the world or of all ages. Like the other primitive axiom of political economy as to land, it fails where "new" countries are occupied by old races. I have already spoken of the strange chance which has unpeopled so great a part of the world just when civilized people wanted to go there. It is strange to think how different would have been the fate of this and of coming generations, if America and Australia had possessed imperfect but thickly populated civilizations, like those of China and of India. In climate, and in all external circumstances, America seems as fit for an early civilization as India; happily, however, it did not possess one, nor did Australia,—there is nothing there now left to cumber the ground. A race rich in the arts of civilization is thus placed in a country rich in unowned but fertile land; and in these countries there is no check on population. Those who can live there—who are the kind of people that can bear the necessary rudeness and can live there—can multiply as fast as they like; they will be able to support their children in the rough

comfort of such countries. Those children will not be in the least likely to die off from want or from disease; on the contrary, they will be as likely to live as any children of the human race. The possible *maximum* of multiplication is there reached, and yet none of the multipliers are deteriorated in the scale of the life, or in any of their circumstances.

And it is necessary to take most careful account of this exceptional case, because it vitally affects the present life of present commercial nations, to which political economy is meant to be an approximation. The existence of those nations is vitally affected by the results of this exception, and therefore those results must not be neglected. It follows from those results that political economy is not the "dismal science" which it was thought to be years ago, and which many people still imagine it to be; it does not teach that of necessity there will be, as time goes on, a greater and greater difficulty in providing for the increase of mankind. It assumes as an indisputable fact a present difficulty; but it does not assume or say that this difficulty will increase. That augmentation of difficulty will not arise, first, because some of the inhabitants of old countries can emigrate to new countries, where people may increase as fast as they can; secondly, because those emigrants produce more than they want in bare subsistence, and can send home a surplus to those who remain behind; thirdly, because even in the old countries the growing improvement in the arts of production is likely at least to counterbalance the inevitable difficulty of a gradual resort to less favored and fertile soils.

This short explanation will, I think, be enough to give a rude idea of the science of political economy in its present form. If I were writing a professed book on the science, there would be much more to be said on the subject. But I hope what has been said will be enough to make plain the rest of this book.

I am to speak of the creators of political economy, and to criticize them; and unless as much as this had been said, the necessary considerations could scarcely have been lucidly explained.

ADAM SMITH AND OUR MODERN ECONOMY.

I.

If we compare Adam Smith's conception of political economy with that to which we are now used, the most striking point is, that he never seems aware that he is dealing with what we should call an abstract science at all. The "Wealth of Nations" does not deal, as do our modern books, with a fictitious human being hypothetically simplified, but with the actual concrete men who live and move; it is concerned with Greeks and Romans, the nations of the Middle Ages, the Scotch and the English, and never diverges into the abstract world. Considering "the natural progress of opulence" as an item in greater studies, as part of the natural growth of human civilization, Adam Smith always thought how it had been affected by human nature taken as a whole.

Adam Smith approximates to our modern political economist because his conception of human nature is so limited. It has been justly said that he thought "there was a Scotchman inside every man." His "Theory of Moral Sentiments," indeed, somewhat differs in tone; but all through the "Wealth of Nations," the desire of man to promote his pecuniary interest is treated as far more universally intense, and his willingness to labor for that interest as far more eager and far more commonly diffused, than experience shows them to be. Modern economists, instructed by a larger experience, well know that the force of which their science treats is neither so potent nor so isolated as Adam Smith thought; they consistently advance as an assumption what he more or less assumes as a fact.

Perhaps a little unfairly, nothing has more conduced to the unpopularity of modern political economists, and to the comparative fame of Adam Smith, than this superiority of their view over his. Of course Adam Smith was infinitely too sensible a man to treat the desire to attain wealth as the sole source of human action; he much overrated its sphere and exaggerated its effect, but he was well aware that there was much else in human nature besides, — as a considerate and careful observer of mankind, he could not help being aware of it. Accordingly he often introduces references to other motives, and describes at length and in an interesting way what we should now consider non-economical phenomena; and therefore he *is* more intelligible than modern economists, and seems to be more practical: but in reality he looks as if he were more practical, only because his analysis is less complete, — he speaks as if he were dealing with all the facts of human nature, when he is not. Modern economists know their own limitations; they would no more undertake to prescribe for the real world than a man in green spectacles would undertake to describe the colors of a landscape. But the mass of mankind have a difficulty in understanding this: they think Adam Smith practical because he seems to deal with all the real facts of man's life, though he actually exaggerates some and often omits others; but they think modern economists unpractical because they have taken the most business-like step towards real practice, — that of dealing with things one at a time.

And it is precisely this singular position of Adam Smith which has given him his peculiar usefulness. He fulfilled two functions. On the one hand, he prepared the way for, though he did not found, the abstract science of political economy. The conception of human nature which underlies the "Wealth of Nations" is near enough to the fictitious man of recent economic science to make its reasonings

often approximate to, and sometimes coincide with, those which the stoutest of modern economists might use. The philosophical and conscious approximation which we now use, has been gradually framed by the continual purification of the rough and vague idea which he employed. In this way Adam Smith is the legitimate progenitor of Ricardo and of Mill: their books would not have been written in the least as they now are, most likely would never have been written at all, unless Adam Smith or some similar writer had written as he has. But on the other hand, Adam Smith is the beginner of a great practical movement too. His partial conception of human nature is near enough to the entire real truth of it to have been assumed as such in his own mind, and to be easily accepted as such by the multitude of readers. When he writes, he writes about what interests most practical men, in a manner which every one will like who is able to follow any sort of written reasoning; and in his time there was a great deal of most important new truth which most practical people were willing to learn, and which he was desirous to teach. It is difficult for a modern Englishman, to whom "Free Trade" is an accepted maxim of tedious orthodoxy, to remember sufficiently that a hundred years ago it was a heresy and a paradox. The whole commercial legislation of the world was framed on the doctrines of Protection; all financiers held them, and the practical men of the world were fixed in the belief of them. "I avow," says M. Mollien, the wise finance minister of the first Napoleon, "to the shame of my first instructors" (the previous officials of France), "that it was the book of Adam Smith, then so little known, but which was already decried by the administrators with whom I had served, which taught me better to appreciate the multitude of points at which public finance touches every family, and which raised judges of it in every household." There were many Free-Traders

before Adam Smith, both writers and men of business, but it is only in the antiquarian sense in which there were "poets before Homer, and kings before Agamemnon": there was no great practical teacher of the new doctrine; no one who could bring it home to the mass of men; who connected it in a plain emphatic way with the history of the past and with the facts of the present; who made men feel that it was not a mere "book theory," but a thing which might be and ought to be real. And thus (by a good fortune such as has hardly happened to any other writer) Adam Smith is the true parent of Mr. Cobden and the Anti-Corn-Law League, as well as of Ricardo and of accurate political economy. His writings are semi-concrete, seeming to be quite so; and therefore they have been the beginning of two great movements, one in the actual and the other in the abstract world.

Probably both these happy chances would have amazed Adam Smith if he could have been told of them. As we have seen, the last way in which he regarded political economy was as a separate and confined speciality: he came upon it as an inseparable part of the development of all things, and it was in that vast connection that he habitually considered it; the peculiar mode of treating the subject which we now have, had never occurred to him. And the idea of his being the teacher, who more than any one else caused Free Trade to be accepted as the cardinal doctrine of English policy, would have been quite as strange to him. He has put on record his feeling:—

"To expect indeed that the freedom of trade should ever be entirely restored in Great Britain, is as absurd as to expect that an Oceana or Utopia should ever be established in it. Not only the prejudices of the public, but what is much more unconquerable, the private interests of many individuals, irresistibly oppose it. Were the officers of the army to oppose with the same zeal and unanimity any reduction in the number of forces, with which master

manufacturers set themselves against every law that is likely to increase the number of their rivals in the home market; were the former to animate their soldiers in the same manner as the latter inflame their workmen, to attack with violence and outrage the proposers of any such regulation, — to attempt to reduce the army would be as dangerous as it has now become to attempt to diminish in any respect the monopoly which our manufacturers have obtained against us. This monopoly has so much increased the number of some particular tribes of them, that like an overgrown standing army, they have become formidable to the government, and upon many occasions intimidate the legislature. The member of Parliament who supports every proposal for strengthening this monopoly is sure to acquire not only the reputation of understanding trade, but great popularity and influence with an order of men whose numbers and wealth render them of great importance. If he opposes them, on the contrary, and still more if he has authority enough to be able to thwart them, neither the most acknowledged probity, nor the highest rank, nor the greatest public services can protect him from the most infamous abuse and detraction, from personal insults, nor sometimes from real danger, arising from the insolent outrage of furious and disappointed monopolists."*

Yet in fact the "Utopia" of Free Trade was introduced into England by the exertions of the "master manufacturers"; and those who advocated it, and who were "thought to understand trade," said that they had learned the doctrines they were inculcating from the "Wealth of Nations," above and beyond every other book.

II.

If we look at the "Wealth of Nations" as if it were a book of modern political economy, we should ask four questions about it:—

(1.) What, by its teaching, is the cause which makes one thing exchange for more or less of other things?

* Book iv., Chap. ii. The last part refers doubtless to the assault on the Duke of Bedford by the silk weavers in May, 1765 (see Horace Walpole's Memoirs, Vol. ii.; Lord Mahon's "History of England," Chap. xliv.; and Vol. iv., page 412, of this edition). — Ed.

(2.) What are the laws under which that cause acts in producing these things? — the full reply to which gives the laws of population and growth of capital.

(3.) If it turns out (as of course it does) that these things are produced by the co-operation of many people, what settles the share of each of those people in those things, or in their proceeds? The answer to this question gives what are called the "laws of distribution."

(4.) If this co-operation costs something (as of course it does, like all other co-operations), who is to pay that cost, and how is it to be levied? The reply to this inquiry is the theory of taxation.

To persons who have not been much accustomed to think of these subjects, these questions may seem a little strange: they will be apt to think that I ought to have spoken of the laws of wealth and of its production and distribution, rather than of the causes which make one thing exchange for more or less of other things, and of the consequent laws. But the truth is, that for the purposes of political economy "wealth" means that which possesses exchange value; and on that ground Archbishop Whately wanted to call the science "catallactics." The air and the sunlight, the riches of nature, are nothing in political economy, because every one can have them, and therefore no one will give anything for them. "Wealth" is not such for economical purposes unless it is scarce and transferable, and so desirable that some one is anxious to give something else for it. The business of the science is not with the general bounty of nature to all men, but with the privileged possessions — bodily and mental powers included — which some have and which others have not.

Unluckily, when we come to inquire what makes these things exchange for more or less of value, one among another, we find ourselves in the middle of a question which involves many and difficult

elements, and which requires delicate handling. Most of the difficulties which are felt in reflecting on the entire subject are owing to a deficient conception of the primitive ingredient; and this will surprise no one conversant with the history of science, for most errors in it have been introduced at the beginning, — just as the questions which a child is apt to ask are in general the ones which it is hardest to answer.

It is usual to begin treating the subject by supposing a state of barter; and this is in principle quite right, for "money" is a peculiar commodity which requires explanation, and the simplest cases of exchange take place without it. But it is apt to be forgotten that a state of barter is not a very easy thing fully to imagine; the very simplicity which renders it useful in speculation makes it more and more unlike our present complex experience. Happily, though barter has died out of the adult life of civilized communities, there remains an age when we, most of us, had something to do with it. To schoolboys, money is always a scarce and often a brief possession, and they are obliged to eke out the want by simpler expedients; the memories of most of us may help them in the matter, though their present life certainly will not.

Suppose, then, that one boy at school has a ham sent him from home (those who object to trivial illustrations must be sent back to the Platonic Socrates to learn that they are of the most special use in the most difficult matters, and be set to read the history of philosophy that they may learn what becomes of the pomposity which neglects them), and suppose that another boy has cake, and that each has more of his own than he cares for and lacks something of the other, what are the proportions in which they will exchange? If boy A likes his own ham scarcely at all, or not very much, and if he is very fond of cake, he will be ready to barter a great deal of it against a little of boy B's cake; and if boy B is

fond of cake too and does not care so much for ham, cake will be at a premium, and a very little of it will go a great way in the transaction, especially if the cake is a small one and the ham a big one; but if on the contrary both boys care much for ham and neither much for cake, and also the ham be small and the cake large, then the ham will be at a premium, the cake at a discount, and both sides of the exchange will be altered. The use of this simplest of all cases is that you see the inevitable complexity of, and that you cannot artificially simplify, the subject. There are in every exchange, as we here see, no less than six elements which more or less affect it in general: first the quantities of the two commodities, and next two feelings in each exchanger, — first his craving for the commodity of the other, and secondly his liking or disinclination for his own. In every transaction, small or great, you will be liable to blunder unless you consider all six.

The introduction of money introduces in this respect no new element. The inseparable use of that incessant expedient is that which ingrains into civilized life the abstract idea of a "purchasing power," — of a thing which, when possessed, will obtain all other things; and independently of the hand-to-hand use of money, this idea of it as a universal equivalent, with the consequent means of counting, has been incalculably beneficial to civilization: but into a mere single interchange its use introduces nothing new. Money in that aspect is simply a desirable commodity; it often happens to be particularly coveted, but at other times, in comparison with some simpler and more essential things, its worth is insignificant.

Nor do the common bargains of commerce contain any additional ingredient: there are always six things to be considered. Suppose that a holder of £10,000 "Peruvians" wants to sell them on the London exchange, the price he will get will obviously

vary with the quantity of Peruvian stock there is about in the market, and the quantity of money which the owners are ready to invest in it; but also according to four other things: —

First. Whether he is anxious for money or not. If he has a bill to meet to-morrow morning and must have money, the chances are great that some one will take advantage of his necessities, and he will have to take less; if on the other hand he be a rich man, — a strong holder, as the phrase is, — he will say, "Ah, if I cannot get my price to-day I will wait till to-morrow," and so he will get a better price.

Secondly. Even if he is not violently in want of money, the price will vary according as he thinks "Peruvians" more or less likely to fall or not. If he thinks them a declining or "treacherous" stock, he will be anxious to get rid of them, and will be less difficult as to price; if he had private and peculiar knowledge that Peru was about to imitate Spain and to stop payment the next day, he will sell at once for any price that those not in the secret would be ready to give him. In these two ways the bargain would be influenced by the mental state of the seller; and it will be influenced in two ways also by the mental state of the buyer.*

Thirdly. If the buyer is desirous of the article, because he thinks it will get rapidly up, he of course will give more than if he thinks it is likely to be stationary, or even for a time to fall; he will "discount" the prospect of improvement, as the market phrase has it.

Fourthly. If he can make little of his money in other ways, say if it is earning 2 per cent., he will be ready to put it into "Peruvians" at a much lower price than he would if he could get 7 per cent. for it in other ways. If there were a crisis, and money had risen in value to 10 per cent., he would hardly

*The collection of tenses in this remarkable paragraph has a characteristically varied beauty which I have not attempted to disturb. — Ed.

put it out of his own control by buying "Peruvians" with it at any price, no matter how low: he would prize the money at such a time, because in a general disturbance it may often be used to untold advantage, or may save its owner from ruin.

In the bargains in all other commodities the same considerations have to be taken account of, and no others. A bargain in foreign stocks or railway shares is in essentials the same as one in corn or cheese: the same six elements are in each case to be thought of, and no others.

Every transaction in commerce is in a legal sense separate; it is a contract in which one side engages to do certain things in return for certain other things which are to be done by the other side: but in a practical sense, most important commercial phenomena are interlaced one with another. The feelings of each seller as to parting or not parting with his goods are mainly caused — or much caused, at any rate — by the amount of goods which other dealers have now in or are about to bring to market, and also by what he imagines to be their "strength" or "weakness," — that is, their more or less of inclination to part with their goods or to retain them, — in every market; and a most able living economist* has justly observed that nowadays this is what we mean by a "market." The estimate formed of all which the dealers have, and of all which they expect to have, is all pretty much collected into one corporate opinion, which floats variously about upon the lips of men, though often it would not be easy to condense into a formula, or to bring it home on evidence to any single speaker. For the most part it is an imbibed, not a discovered fact, that the market is "dull, and likely to be dull," "lively, and likely to be so;" these are in part truths of observation, but in part also accredited hypotheses, — a market knows its own present state, and anticipates

* Professor Jevons's "Theory of Political Economy," page 85.

its own future, by signs which an outside observer would not see, and by the unconscious contribution of many minds to a daily growing opinion. A market in the higher commercial sense of the world*— in the sense in which we speak of the "money market" — does not mean, as it once did, a place where goods are exposed, but a historical result of the proximity of traders; a set of dealers cognizant of one another, and acquainted more or less with each other's position and each other's intentions.

It must not be supposed, however, that the process of bargain-making approaches in general to a statistical calculation. A person proposing to buy, looks at a trade circular to see what the writer of it thinks the price is; he asks the broker what price has been given, what offered, what refused; he inquires whether holders are strong or weak, whether they are under-supplied or over-supplied; he asks if other buyers are many or few, whether they are eager or indifferent, whether they have much money or whether they have little: and out of these inquiries he forms an idea of the price at which he is likely to buy the commodities. A person intending to sell a commodity forms in like manner a notion of the price he is likely to obtain for it; on the surface the appearance is often frivolous enough. Many persons go about inquiring, "In what state do you think the market, sir?" and getting, as it would seem, not much reply in return; but underneath there are some of the keenest anxieties and most ardent hopes of human nature. A large quantity of goods is on the market, by selling which many holders must live, if they live at all; a great though uncertain quantity of money is in the market, which the owners mean to live by investing: the main interest of many lives is at stake, and the subsistence of many families, little as on the outside the market looks so.

*An evident misprint for "word."—Ed.

On the whole, then, we may sum the matter up thus:—

First. That a bargain will be struck when four conditions are satisfied, viz.:—

When the seller thinks he cannot obtain more from the buyer with whom he is dealing, or from any other;

When he is sufficiently desirous to sell his article, or enough in want of money, to take that price;

When the buyer thinks that he cannot obtain the article for less, either from that seller or from any one else;

When he is so eager for the article, or so anxious to invest his money, as to give it.

Secondly. That every bargain is a datum for other bargains, and influences the opinions on which they are based.

Thirdly. That the average price of such bargains is the market price.

Fourthly. That the main elements of market price are those which prevail in most bargains; viz., the actual quantity of the article in the market, the quantity of money actually ready to be invested in it, and the average strength with which the wish to hold the article, the wish to acquire it, the wish to obtain money and the wish to invest it, operate through the whole class of buyers and of sellers.

These formulæ may seem complex, but I do not think that any of them can be left out or shortened except by omitting necessary facts.*

An attempt is indeed commonly made to abbreviate these rules; very much the same is meant by the common phrase that market price is determined by "supply and demand," which is a good phrase enough when you know how to manage it. But the effect of using so few words for so much meaning is, that they are continually being used in various senses; no one signification of the terms can be

* See Appendix.

stretched over the whole matter: and in consequence, a literature has come to exist discussing their ambiguities. The most obvious objection is, that if the words are taken in their natural sense they imply a relation between two things of wholly different natures: demand is a desire in the mind, supply a quantity of matter; how then can there be an equality between them? And even when "demand" is used in the best sense,* for the quantity of money or purchasing power, the formula has the defect of mentioning only the two quantities of the changing commodities, of not saying that they are only estimates of quantities, and of not warning those who use it that they must likewise consider the other elements, — the four wishes of the two exchangers.

It is most important to be clear upon the matter, because confusion about it has led and still leads to many most mischievous fallacies. For example, it has been vigorously argued that trades-unions could not alter the price of labor: "The supply, the number of laborers," it was said, "is the same as before, and also the demand, viz., the quantity of money wanting to buy labor: the two causes being thus identical, the effect cannot be different." But in fact a trades-union establishment at once alters the mental conditions: it turns the laborer, in the Stock Exchange language, from a weak holder into a strong one; it enables him to hold. Before, he must either take the master's terms or starve; now he has money to live, and will often get more, because he can stand out for a good bargain.

The complete view of the facts thus effaces at once the ingrained mistake of the last generation, and it also destroys as quickly a recent error now common. It is imagined that because trades-unions

*See the admirable dissertation of Professor Cairnes, "Leading Principles," pages 17-40. A most ingenious collection of the difficulties of the doctrine of supply and demand as usually stated will be found in "Thornton on Labor," Book ii., Chap. i. — B.

have sometimes raised wages to some extent, they can raise them, at any rate gradually, to any extent; but we now see the limit of their power. They can only win when the funds of the union are stronger than the funds of the capitalists; and this will sometimes be so and sometimes not be so. A clear view of the facts also explains (that which is a difficulty in the ordinary theory) the difference between a speculative market and an ordinary one: so long as it is imagined that market price is determined by the supply of the article in the market and the money here eager to buy it, it is not possible to explain why two markets in which both these elements coincide should be so different as a dull market and an excited one always are; but as soon as we understand that we have to deal likewise with opinions and with wishes, we see how there is great scope for discrepancy and for mutability.

Again, on another side of the subject, it has been incessantly said that (at all events since the Act of 1844, which limits the power of issue) the Bank of England cannot alter the rate of discount: there exist, it is said, a certain number of bills and a certain amount of money ready to be invested in bills, and this determines the way in which one will be exchanged for the other. But in fact, much of such money is held by the Bank of England, and the fact of its being unwilling to lend inevitably alters the "equation of exchange": the desire of the principal dealers to operate or not to operate is a vital element in every market. When you read in the jargon of trade circulars that "yarns are sluggish," and that "teas are lively," the palliation for the use of these ridiculous adjectives is, that in the facts described there is as much of mental state as of physical supply.

It is in consequence of the extreme importance of these mental elements that in all markets you hear so much of "flying and often concocted rumors." On the Stock Exchange "the lie of the day," as

Dr. Johnson would have called it, always has some influence, because the momentary wishes of sellers to sell and buyers to buy are greatly affected by what they hear as to possible wars and revolutions of the nations whose debts they are buying and selling. The best states only care for such rumors at critical instants; but more or less the reputes of minor ones lie at the "truth of him that makes it," and their credit is incessantly talked up and talked down much more than they themselves desire.

The league of the moment — "rig," "ring," "syndicate," or "pool," or what not, "one form with many names" — operates in the same way: it is a mental* expedient for changing the mental state of the market. By combining, the same persons are able to make the same amount of speech and the same amount of money go further. They affect opinion more, because they say the same things; and they are more tenacious holders or more desperate buyers, because they rely one on another.

We see too from this analysis why it is that one man is a good seller and another a bad one. A good seller is a good advocate, who acts effectually on the opinions and feelings of persons inclined to deal with him: who makes them think that the article is very excellent; that it is growing very scarce, that it is going to be scarcer; that a great many people are wanting it, that much money is going to be had for it; that the holders in general are anxious not to sell as yet, because they believe it will get dearer; that he himself is above all unwilling to part with his article, and will do so only as a personal favor: he weakens the judgment and intensifies the desire of his opponent as he wishes.

The requisites of a good buyer are in essentials the same: he also is an advocate, only on the other side. He has to show that the article in question is

* The adjective is meaningless and probably a slip of the pen: a temporary "ring" is no more "mental" than a permanent partnership. — Ed.

undesirable, that it is plentiful, that most holders are most anxious to sell it; that few persons, and those with little money, are coming forward to buy it; that though perhaps he might himself be induced to buy a little of it, yet it would only be under peculiar circumstances and as a matter of private feeling. There is indeed a common saying that a good buyer is much rarer than a good seller; and I believe that the Manchester warehouse-keepers, as they are called, — that is, the great dealers in underclothing: great traders, but who do not produce anything, and must therefore both largely buy and sell — give higher salaries to their buyers than to their sellers. But this is only because the buyers are the advocates who have to address the more skilled audience; they buy of a few manufacturers who understand business well, and must therefore be careful what they say. The sellers for the firm, who distribute the goods among the country shops, have people of very inferior intelligence to deal with. A few good buyers, therefore, purchase what many less qualified sellers dispose of; but in its essence the business is identical, — it consists in exciting desire and in modifying opinion.

It may strike some people that if prices thus depend on casual opinions and on casual desires, it is odd that prices in markets should be so uniform on particular days in particular markets as they really are; but in fact, at ordinary times, these casual opinions and casual desires form a sort of average. The timid seller is emboldened by knowing that others are courageous, the necessitous by knowing that others are strong; the cautious buyer is forced on because he knows that eager ones will outstrip him, the adventurous is restrained because he knows that others have doubts: and so on through the whole subject. In the infancy of trade, no doubt there is ample room for great variations. A most graphic observer has said of Oriental markets: —

"The necessities of a savage are soon satisfied; and unless he belongs to a nation civilized enough to live in permanent habitations, and secure from plunder, he cannot accumulate, but is only able to keep what he actually is able to carry about his own person. Thus the chief at Lake N'gami told Mr. Andersson that his beads would be of little use, for the women about the place already 'grunted like pigs' under the burden of those that they wore, and which they had received from previous travelers."*

But in civilized times facts are known, advocacy is weak, and prices are usually uniform. But they are not so at a commercial crisis; then, as the phrase goes, prices are very "wide." A necessitous seller must sell, and he pulls down the price for an instant; but if a buyer is stimulated by this, and wants to buy more at the same price, he will find that he cannot do it. There are no more equally necessitous sellers in the market; the rest do not want money for the instant, and will not sell except at a much higher price. At such a moment, too, skillful people will act on the fears of others: I have heard it said of a bland and delicate operator, who was ultimately very successful, that at critical times "he *encouraged* others to be frightened"; and in panics, cool heads and strong nerves make much by dealing with weak nerves and hot heads. But in common times the contrary tendencies are subdued to an average; the most anxious seller will depress a good stock but very little, and the most eager will raise it but a little also.

I have been obliged to state the facts carefully, before discussing Adam Smith's doctrine, because I could not otherwise make an attempt to estimate it intelligibly; and I must go on with some further facts also, or even that estimate would be broken and faulty. At a glance, it is plain that the doctrine of exchange which I have sketched cannot be the final theory: it depends on the relative quantity of two things; but as most things can be increased at

*Galton's "Art of Travel," under "Presents and Articles for Payment."

will by human labor, men have therefore in most cases the means of making these quantities what they please, and therefore these quantities cannot be ultimate causes. "Supply and demand" cannot be final regulators of value; for in most cases men can supply what they like, and to finish the subject we must know when they will begin to do so and when they will leave off.

The first answer to be given to these questions is, that producers who produce, in order to receive something in exchange for their products, will go on producing as long as the gain, pleasure, satisfaction (whatever word you choose to use) they receive from that something is a sufficient compensation to them for the *bore* and irksomeness of production, and they will stop producing when it ceases to be sufficient. In an early state of society it is easy to imagine simple cases of this. In the times of which the Scandinavian "kitchen-middings" are the only extant vestige, the population lived partly by hunting and partly by fishing: most, I suppose, did both; some confined themselves to that which they did best. In that case a hunter who only hunted would work as long as the fish received in exchange seemed to him to repay the trouble of hunting; a fisherman who only fished would do the same. The man who tattooed the population would continue to do so as long as the game or the fish he received in return seemed to make it worth his while. The polisher of flint implements or bones would do just the same. The essence of the whole is the exchange of the produce of much labor and very little capital, so long as the laborer thinks what he thus obtains repays him for his labor. And the same thing goes on down to the end of civilization in a subordinate way: an old woman gathers laver on the sea-shore of Somersetshire as long as any one will give the pittance she expects for it; a diver will bring up pearls as long as any one will give what he thinks

is enough to make it worth while to go to the bottom of the sea for them. The primitive form of production still exists, and the primitive estimate of recompense; but in most cases they exist as "survivals" only. In two remarkable instances, of which I shall speak hereafter, they still alter the main tide of commerce: but for the most part the interest of the transactions is principally antiquarian, — little money is now made by them; but they are worth thinking of now and then, because they remind us of what once was the only way in which the relative value of commodities was finally determined in the world.

But the main part of modern commerce is carried on in a very different manner; it begins at a different point and ends at a different point. The fundamental principle is indeed the same: the determining producer — the person on whose volition it depends whether the article shall be produced or not — goes on so long as he is satisfied with his recompense, and stops when he ceases to be so satisfied. But this determining producer is now not a laborer but a capitalist: in nine hundred and ninety-nine cases out of every thousand, it is the capitalist and not the laborer who decides whether or not an enterprise shall be commenced, and therefore whether the consequent commodity shall come on the market; he buys his labor just as he buys his raw material. He may calculate wrongly in both cases; he may think he will buy when labor or material is cheaper than it turns out that he can [buy them]: but his calculation will be the critical element in the whole business, — that which decides whether it shall or shall not be entered upon.

This change has occurred in the organization of industry, because the new mode of organizing it is infinitely more efficient than the old. A body of separate laborers has many of the characteristics of a mob; but one acting under the control of a capitalist

has many of those of an army. A capitalist provides his laborers with subsistence, directs each what he shall do and when, and educes the desired result of the whole combination at the proper time, much as a general does; he and his men will live and will produce riches where a mere multitude of laborers will starve. When, in very modern times, it has been endeavored in schemes of "co-operation" to enable laborers to subsist without dependence on an individual capitalist, it has been necessary, under cloak of the combination, to invent a capitalist in disguise. A common fund subscribed beforehand, an elected board to invest it, a selected manager to combine it, are all refined expedients for doing in a complex way what the single rich capitalist does in a simple way; even yet we do not know how far they can be applied with comparable efficiency. In simpler times, the rich man who has much beforehand buys the labor of his poorer neighbors who have nothing, and directs their power towards results which no one of them could perhaps have conceived, and which a thousand times as many, without his controlling mind, would have been impotent to produce. On one point, however, — the point which is most material for the present purpose, — the old organization or disorganization of mere laborers acting separately, and the exact modern industry where enterprise depends on the *fiat* of the capitalist, are alike, and are so because human nature is alike both in capitalist and laborer: neither of them will take much trouble to obtain in one way that which he can obtain with very little trouble in another way. As far as labor can migrate from employment to employment, articles produced by the same labor will exchange for one another: if it were not so, the laborers who worked at the thing which fetched least would be throwing away some of their labor; they would do better to produce something else, and in the end they would do so. In the same way, as

far as capital (including the capital which buys labor) can be transferred from employment to employment, things produced with the same amount of capital, in similar times and similar circumstances, exchange one for another; when it is not so, capital tends to go from the pursuit[s] in which it is less profitably employed to those in which it is more so.

As might be expected, the modern organization is much more perfect in this respect as in most others; labor always circulates from employment to employment.

"Whatever," says Adam Smith, "obstructs the free circulation of labor from one employment to another obstructs that of stock likewise; the quantity of stock which can be employed in any branch of business depending very much upon that of the labor which can be employed in it. Corporation laws, however, give less obstruction to the free circulation of stock from one place to another than to that of labor; it is everywhere much easier for a wealthy merchant to obtain the privilege of trading in a town corporate, than for a poor artificer to obtain that of working in it.

"The obstruction which corporation laws give to the free circulation of labor is common, I believe, to every part of Europe. That which is given to it by the poor laws is, so far as I know, peculiar to England: it consists in the difficulty which a poor man finds in obtaining a settlement, or even in being allowed to exercise his industry, in any parish but that to which he belongs. It is the labor of artificers and manufacturers only of which the free circulation is obstructed by corporation laws; the difficulty of obtaining settlements obstructs even that of common labor."*

Man is of all pieces of luggage the most difficult to be removed. In general an ill-paid laborer early in life gives hostages to misfortune,†—he burdens himself with the support of a wife and children; he cannot move, or they would starve. But civilization has invented an elaborate machinery for holding capital in a transferable form. The basis of this machinery is the invention of money; one of the

* Book i., Chap. x.

† "He that hath wife and children hath given hostages to fortune."—Bacon, Essay on Marriage.

uses of money is, that it is a mode in which capital may be held without loss in what may be called a "provisional" form. All capital originally comes from production,—is, say, so much corn or tin or hemp; but if a man holds corn or any other commodity, he may not be able to exchange it in a little while for so much as he can to-day,—most commodities are in their nature perishable, and most others are liable to depreciation from the change in human desires. But money is always wanted, for it will buy everything; any one who is not sure how he will ultimately employ his capital can hold it in the form of money. This provisional state—this interval of non-employment—is a great security for the substantial equality of equal capitals in equal employments; for it gives capitalists time to look before them and see what they should select because it will yield most, and what they should avoid because it will yield least.

But in this its elementary form, the machinery for holding capital (so to say) in expectation has an obvious defect: the capitalists derive no income from it while it is in a state of indecision. "Money" is barren, according to the old saying, and whoever holds mere coin will certainly derive no income. But in countries where banking is well developed, the machinery is far more efficient: a man who has capital lying idle can place it with a banker, who, if he will agree to give some notice before he withdraws it, will agree to pay him some interest on it. This interest, as far as it goes, is a source of income during the period of suspended investment, and is something on which the capitalist can subsist without trenching on his capital, and without hurrying to a premature use of it. This capital awaiting investment the banker employs in the same way that he employs the unused balances of people's income; and that is, in lending to the trades which are at the moment most profitable. As I have elsewhere explained:—

Political economists say that capital sets towards the most profitable trades, and that it rapidly leaves the less profitable and non-paying trades; but in ordinary countries this is a slow process, and some persons who want to have ocular demonstration of abstract truths have been inclined to doubt it because they could not see it. In England, however, the process would be visible enough if you could only see the books of the bill-brokers and the bankers: their bill cases as a rule are full of the bills drawn in the most profitable trades, and *cæteris paribus* and in comparison empty of those drawn in the less profitable. If the iron trade ceases to be as profitable as usual, less iron is sold; the fewer the sales the fewer the bills: and in consequence the number of iron bills in Lombard Street is diminished. On the other hand, if in consequence of a bad harvest the corn trade becomes on a sudden profitable, immediately "corn bills" are created in great numbers, and if good are discounted in Lombard Street. Thus English capital runs as surely and instantly where it is most wanted, and where there is most to be made of it, as water runs to find its level.*

In this way "expectant capital," while it is so expectant, forms part of a fund which is lent now to this trade and now to that, according as for the moment each trade is more profitable; and at last, instructed by reflection, its owner will invest it, other things being equal, in the trade which offers the most for it. In its temporary use it tends to equalize temporary profits; in its permanent use it does so too.

No doubt some callings are naturally pleasant, others unpleasant; some encouraged by opinion, others adverse to it; some easy to learn, some difficult; some easy to enter, others hedged in by tradition and privilege; some abounding in risk, some with little of it: but our principle is not affected by these. It is that, non-pecuniary encouragements and discouragements being reckoned, capitals employed in all trades yield an equal return in equal times.

What that return will be, it would be premature here to speak of. It is only necessary to say that it is such as the capitalist will think worth while

* See pages 10, 11 of this volume.

to invest his capital for, — enough, that is, to compensate him for the inevitable trouble and attendant risk; if it is not enough, he will let it continue uninvested at interest, or will eat it up and live on it.

We must carefully bear in mind, too, that the rule that equivalent returns are made to equal capitals in the same times is only true of employments between which capital fluctuates freely. This is to an almost perfect extent true of employments in this country, and to a great extent, though far from an equal extent, to the employments of its own country.* But it is not at all true of employments in different countries: English capital, by far the most locomotive of all capitals, will not go abroad for the same percentage of return that will suffice it at home. A great deal of the capital of all countries — by far the greater part of it everywhere, indeed — could hardly on any terms be tempted abroad. We have arrived, however, at the principle that within the same nation all commodities will tend to be of the same exchangeable value whose cost of production is identical; and that this cost of production is that which the capitalist expends, and the return for which he is willing to take the pains of expending it.

And this will be enough for our present purpose.

III.

On all these subjects Adam Smith wrote in an extinct world, and one of the objects always before him was to destroy now extinct superstitions. In that age it was still believed — though the belief was dwindling away — that wealth consisted in "money," and that its value was somehow different from that of anything else. As Adam Smith himself describes it: —

"That wealth consists in money, or in gold and silver, is a popular notion which naturally arises from the double function of money, as the instrument of commerce and as the measure of value. In consequence of its being the instrument of commerce,

*Read "to all employments within their own country." — Ed.

when we have money we can more readily obtain whatever else we have occasion for than by means of any other commodity. The great affair, we always find, is to get money; when that is obtained, there is no difficulty in making any subsequent purchase. In consequence of its being the measure of value, we estimate that of all other commodities by the quantity of money which they will exchange for. We say of a rich man that he is worth a great deal, and of a poor man that he is worth very little, money. A frugal man, or a man eager to be rich, is said to love money; and a careless, a generous, or a profuse man is said to be indifferent about it. To grow rich is to get money; and wealth and money, in short, are in common language considered as in every respect synonymous."*

No true theory of "value" could be established till this false theory was cleared away; so long as even a vestige of it haunts the minds of thinkers and learners, they cannot think or learn anything on this subject properly: and therefore Adam Smith applies his whole force to the confutation of it. His success has been so complete that it has made this part of his writings now useless: no one now thinks or supposes that money is the essence of wealth; that it is anything but a kind of wealth, having distinct uses, like other kinds. The strongest interest in reading the chapters of the "Wealth of Nations" on the subject is given by the vigor with which they are written. They are essentially models of practical writing: they are meant to extirpate living error; they follow that error into the minds of those who believe it, and extirpate it in the forms in which it thrives and rules there. The error that the precious metals are the only real wealth was a living error to Adam Smith, for he had lived with many persons who held it.

The efficacy of Adam Smith's refutation is not wholly derived exactly from its literary merit. Hume had before given a brief exposure, which in mere writing is at least as good; but Hume impressed on this, as on so much else, a certain taint of paradox.

* Book iv., Chap i.

He seems to be playing with his subject; he hardly appears to believe what he says, and a plain reader is often puzzled to know whether he ought to believe it either. On a strong-headed man of business, semi-insincere exposition produces no effect. But Adam Smith takes up the subject in a solid straightforward way, such as he knew would suit the Glasgow merchants with whom he had once lived; and he talks to them, not only as a man acquainted with present mercantile things, but also as one possessing much other culture and authority. He impressed practical men by his learning, at the same time that he won them by his lucidity and assured them by his confidence.

But when we pass from the refutation of ancient errors to the establishment of coherent truth, we shall not be equally satisfied. Students are indeed still sometimes told that they will find such truth in Adam Smith; but those who had nothing else to read, and who wanted to read accurately, did not find it so. What in fact a student will find in Adam Smith is a rough outline of sensible thoughts; not always consistent with themselves, and rarely stated with much precision; often very near the truth, though seldom precisely hitting it: a great mental effort in its day, though always deficient in the consecutiveness required by careful learners, and except for the purpose of exciting an interest in the subject, altogether superseded and surpassed now.

"Gold and silver, however," says Adam Smith, "like every other commodity, vary in their value; are sometimes cheaper and sometimes dearer, sometimes of easier and sometimes of more difficult purchase. The quantity of labor which any particular quantity of them can purchase or command, or the quantity of other goods which it will exchange for, depends always upon the fertility or barrenness of the mines which happen to be known about the time when such exchanges are made. The discovery of the abundant mines of America reduced in the sixteenth century the value of gold and silver in Europe to about a third of what it had been before. As it cost less labor to bring those metals from the mine

to the market, so when they were brought thither they could purchase or command less labor; and this revolution in their value, though perhaps the greatest, is by no means the only one of which history gives some account. But as a measure of quantity, such as the natural foot, fathom, or handful, which is continually varying in its own quantity, can never be an accurate measure of the quantity of other things; so a commodity which is itself continually varying in its own value can never be an accurate measure of the value of other commodities. Equal quantities of labor, at all times and places, may be said to be of equal value to the laborer. In his ordinary state of health, strength, and spirits, in the ordinary degree of his skill and dexterity, he must always lay down the same portion of his ease, his liberty, and his happiness. The price which he pays must always be the same, whatever may be the quantity of goods which he receives in return for it. Of these, indeed, it may sometimes purchase a greater and sometimes a smaller quantity; but it is their value which varies, not that of the labor which purchases them. At all times and places that is dear which it is difficult to come at, or which it costs much labor to acquire; and that cheap which is to be had easily, or with very little labor. Labor alone, therefore, never varying in its own value, is alone the ultimate and real standard by which the value of all commodities can at all times and places be estimated and compared. It is their real price; money is their nominal price only."*

But in the present day it is not true at all that things are dear simply in proportion to the mere labor which it has cost to produce them: a thousand men's labor assisted say by ten steam engines will produce many more valuable things than a thousand men's labor without those steam engines; the result of the labor of the two sets of men will not exchange for one another at all. Besides immediate labor, there is a vast apparatus of the assisting results of past labor; these must be paid for in some way, or their owner will not let them be used. There is something else essential to modern industry besides labor; and that is *saving*, or the refraining from the immediate consumption of past labor. Sometimes this saving is used to co-operate with labor as in

* Book i., Chap. v.

machines, some times to support it as with food and necessaries; but in either case its existence must be remunerated and its use paid for. As modern economists say, the value of an article must be such as to compensate not only for the labor but for the *abstinence* by which it was produced.

Again, Adam Smith speaks of the quantity of labor which a commodity will buy, as if it were identical with the quantity of labor by which it was produced. He says: —

"Every man is rich or poor according to the degree in which he can afford to enjoy the necessaries, conveniences, and amusements of human life. But after the division of labor has once thoroughly taken place, it is but a very small part of these with which a man's own labor can supply him. The far greater part of them he must derive from the labor of other people; and he must be rich or poor according to the quantity of that labor which he can command, or which he can afford to purchase. The value of any commodity, therefore, to the person who possesses it, and who means not to use or consume it himself, but to exchange it for other commodities, is equal to the quantity of labor which it enables him to purchase or command. Labor, therefore, is the real measure of the exchangeable value of all commodities.

"The real price of everything — what everything really costs to the man who wants to acquire it — is the toil and trouble of acquiring it. What everything is really worth to the man who has acquired it, and who wants to dispose of it or exchange it for something else, is the toil and trouble which it can save to himself, and which it can impose upon other people. What is bought with money or with goods is purchased by labor as much as what we acquire by the toil of our own body. That money or those goods indeed save us this toil: they contain the value of a certain quantity of labor, which we exchange for what is supposed at the time to contain the value of an equal quantity. Labor was the first price, the original purchase money that was paid for all things. It was not by gold or by silver, but by labor, that all the wealth of the world was originally purchased; and its value, to those who possess it, and who want to exchange it for some new productions, is precisely equal to the quantity of labor which it can enable them to purchase or command."*

*Book i., Chap. v.

But the quantity of labor which a thing will purchase depends on the degree in which it is desired by laborers: a grand piano in a coarse community will buy less labor than a barrel of beer. Mere labor is the worst "measure" of value conceivable, because it varies with the appetites and differs with the tastes of mankind. There is nothing more uncertain, more changeable, or more casual than the number of days' labor that an article will purchase; as some one expressed it, "Gin will purchase more than it ought, and tracts less than they ought."

Adam Smith did not put the matter graphically enough before his mind. He speaks of a man's fortune being equal "to the quantity either of other men's labor, *or, what is the same thing,* of the produce of other men's labor, which it enables him to purchase or command."* But unless you suppose that some general instrument of purchasing power, like money, exists, and that a man's fortune consists in it, the two things are not the same at all. One man's fortune may consist of a valuable library, which would buy no manual labor at all, but for which bookish people would barter many other commodities; another may have a heap of coarse meat and drink, which will bring crowds of laborers to share them, but for which few refined persons would give anything.

Unquestionably, as has been shown, in a rude state of society, where labor is the principal cost of production, two articles produced with the same amounts of labor will tend to exchange one for another, because every laborer will tend to migrate to the place where his labor is better rewarded and leave the place where it is worse. And this is what Adam Smith vaguely saw, and several times meant to say, but he did not exactly say it; he never says it, and often says something quite different.

* Book i., Chap. v.

In another passage Adam Smith sets forth a similarly vague view of the doctrine of exchangeable value as it stands after capital has accumulated. But as will be shown, he does not work it out fully; and he does not reconcile it, or feel that there is a difficulty in reconciling it, with his former doctrine of value based on mere labor, and yet they are plainly incompatible.

"There is," he says, "in every society or neighborhood an ordinary or average rate both of wages and profit in every different employment of labor and stock. This rate is naturally regulated, as I shall show hereafter, partly by the general circumstances of the society, their riches or poverty, their advancing, stationary, or declining condition; and partly by the particular nature of each employment.

"There is likewise in every society or neighborhood an ordinary or average rate of rent, which is regulated too, as I shall show hereafter, partly by the general circumstances of the society or neighborhood in which the land is situated, and partly by the natural or improved fertility of the land.

"These ordinary or average rates may be called the 'natural rates' of wages, profit, and rent, at the time and place in which they commonly prevail.

"When the price of any commodity is neither more nor less than what is sufficient to pay the rent of the land, the wages of the labor, and the profits of the stock employed in raising, preparing, and bringing to market, according to their natural rates, the commodity is then sold for what may be called its 'natural price.'

"The commodity is then sold precisely for what it is worth, or for what it really costs the person who brings it to market; for though in common language what is called the 'prime cost' of any commodity does not comprehend the profit of the person who is to sell it again, yet if he sells it at a price which does not allow him the ordinary rate of profit in his neighborhood, he is evidently a loser by the trade; since by employing his stock in some other way he might have made that profit. His profit, besides, is his revenue, the proper fund of his subsistence. As, while he is preparing and bringing the goods to market, he advances to his workmen their wages or their subsistence; so he advances to himself in the same manner his own subsistence, which is generally suitable to the profit which he may reasonably expect from

the sale of his goods. Unless they yield him this profit, therefore, they do not repay him what they may very properly be said to have really cost him.

"Though the price, therefore, which leaves him this profit, is not always the lowest at which a dealer may sometimes sell his goods, it is the lowest at which he is likely to sell them for any considerable time; at least where there is perfect liberty, or where he may change his trade as often as he pleases."*

As every one will see, this second doctrine is much more like real life than the former; but in Adam Smith's mind it did not supersede it. All through the "Wealth of Nations" there is recurring confusion between three things, — the "natural price" of an article estimated as in the above passage, the quantity of labor required to make it, and the quantity of labor which it will buy; of which three things, no one ever for the most part coincides with the others.

Even this second exposition contains one error, which unfits it for scientific use, and which the sharp eye of Hume at once perceived: "I cannot think," Hume wrote, "that the rent of farms makes any part of the price of produce." And very clearly it does not; for if it does, of what farm? The rent of various pieces of corn-growing land varies infinitely: is it the rent of the dearest which enters into the price of the half-and-half, or of the cheapest? We know that the price of corn is the same, no matter on what quality of land it is grown: does that price pay the rent of good, of indifferent, or of bad land? This question Adam Smith does not answer, nor seemingly does the necessity of answering it occur to him.

On the other hand, it must be owned that there is a great naturalness in Adam Smith's idea; it is that which would strike every one on a first view of the facts. The capitalist pays the rent of the

*Book i., Chap. vii.

land, just as he pays the wages and buys the seed corn; and it is as much necessary that he should be recouped for the payment of that rent as for either of the other payments. If the "rent" of the farm is not an element in the price of the corn, how then is that rent to be paid?

The answer is, that the rent of extra-good land is paid out of the extra quantity (or extra-good quality) of what it produces. If one acre of land yields twice as much as another, it will answer the capitalist's purpose to pay twice as much for its use. But if he does pay twice as much, the cost at which he will grow each ear of corn will be the same as that of the farmer on less good land; the extra fertility will be compensated by the extra rent. It may of course be that the owner of the best land will farm it himself, and then he will have no rent to pay for its unusual goodness; but he will not sell his produce the least cheaper for that,—he will get all which he can for it. We have seen how "market price" is determined: it depends on certain desires of the seller and the buyer,—in part generated by the quantity of the article and the quantity of money, and in part not. But none of those desires would make a man say, "I produce this at a less cost than others, and therefore I will let them charge a higher price than I do." No producer sets himself to introduce fairness into the reward of production, by letting those who possessed less facilities than he did, receive more than he does: the nature of market-going man is formed quite differently.

The only reason why the cost of production in the end tends to determine market value is, that every one who wants an article will take the easiest means to get it. If a capitalist wants to invest his money to gain an income, he will, *cæteris paribus*, be apt to engage in pursuits which are reputed profitable, and to avoid those which are reputed unprofitable; and this will reduce the profits of all trades not *to*

a level, but *towards* a level. But the argument assumes that all means of production are equally open to every one. If any one has exclusive possession of an especially good opportunity, he will get something out of it proportioned to that especial goodness. The owner of extremely good land, who farms it himself, will get a return over and above the ordinary rate of profit in proportion to that goodness; he will sell a great deal at the price which will yield the required profit to those who can sell only much less.

This is only another way of saying that the capital which yields the least permanent return — the least profit for which farmers as a class will carry on agriculture — is that which determines the price of agricultural produce. This is the least which the farmer in the long run will sell for, and the most which he will be able to obtain; and this capital is that which pays the least rent.

In all countries where land is easily accessible to capital, that "least" rent is *no* rent: because land is taken into cultivation as soon as its cultivation will pay the usual profit; and because after it is in cultivation, more and more capital is expended upon it, so long as expenditure meets with the usual return. The production of valuable things on the surface of the ground is exactly like the extraction of valuable things from beneath that surface: it is the worst mine which can in the long run be kept going that in the long run determines the price of the produce. The owner of the better mine does not sell his ore cheaper than his neighbor, because he can get that ore at less cost than his neighbor; the best circumstanced miner exacts as much as the worst circumstanced miner is able to obtain. And the "worst circumstanced" mine pays no royalty to the owner at all; it only pays a bare profit on the capital.

Adam Smith's idea, therefore, that in ordinary circumstances the rent of land entered as an element

into the price of agricultural produce, though a very natural idea, was a complete mistake; because he could not have told what rent he meant, — the rent of best or middling or bad land, — and because much capital employed in agriculture yields only the ordinary profit on capital, and therefore pays no rent at all. The mode of estimating "cost of production," given by Adam Smith, in this case was most imperfect; because one of its terms was undetermined, — a variable which might be anything, and often is nothing.

This opinion of Adam Smith's as to the rent of land is closely connected with a peculiar opinion of his as to agriculture: he held that it was the most profitable employment to which the capital and industry of a country could be directed. This opinion, like many of his others, was a modification of that which he had learned in France. The *économistes* in Paris at that time held that agriculture was the only profitable occupation of labor and capital; and it would take many pages to give an account in the least comprehensible, of the elaborate reasoning by which they had persuaded themselves of this ridiculous result.* Adam Smith of course rejected it, — his strong sense particularly revolted from that kind of argumentative absurdity; but he was nevertheless influenced by it, — though he did not hold agriculture to be the only source of profit, he held that it was a particularly prolific one. "It keeps three people," he would have said, "the landlord, the capitalist farmer, and the laborer; manufacturers and trade keep only two, the laborer and capitalist: clearly therefore agriculture has the advantage." He assigned at length what he thought was the philosophical reason: —

"The laborers and laboring cattle, therefore, employed in agriculture, not only occasion, like the workmen in manufactures, the reproduction of value equal to their own consumption, or to the

* See Vol. iii., pages 291-3.

capital which employs them, together with its owner's profits, but of a much greater value: over and above the capital of the farmer and all its profits, they regularly occasion the reproduction of the rent of the landlord. This rent may be considered as the produce of those powers of nature, the use of which the landlord lends to the farmer. It is greater or smaller according to the supposed extent of those powers; or in other words, according to the supposed natural or improved fertility of the land. It is the work of nature which remains after deducting or compensating everything which can be regarded as the work of man. It is seldom less than a fourth, and frequently more than a third, of the whole produce. No equal quantity of productive labor employed in manufactures can ever occasion so great a reproduction: in them nature does nothing, man does all; and the reproduction must always be in proportion to the strength of the agents that occasion it. The capital employed in agriculture, therefore, not only puts into motion a greater quantity of productive labor than any equal capital employed in manufactures, but in proportion too to the quantity of productive labor which it employs, it adds a much greater value to the annual produce of the land and labor of the country, to the real wealth and revenue of its inhabitants. Of all the ways in which a capital can be employed, it is by far the most advantageous to the society."*

Probably few passages in so eminent a writer, on the subject for which he is eminent, contain so much curious falsehood. If nature does nothing in manufactures, in what is it that it does anything? "Manufactures" are but applications of natural forces, just as agriculture is another application; and the reasoning assumes that the natural causes which produce *dear* things are more beneficial to mankind than those which produce *cheap* things,—though had Adam Smith seen that he was making such an assumption, he would have been the first to reject it. The causes which produce dear things are not necessarily more beneficial than those which produce cheap ones; they are only less plentiful. A diamond mine is not more useful to the state than a coal mine; probably in the strictest sense of

* Book ii., Chap v.

the word not so useful. The fact that a particular occupation keeps three classes of men, while other occupations only keep two, only shows that there is a special difficulty in getting into that occupation and a special scarcity in its opportunities; it proves nothing as to the degree of good which it does for the public. And Adam Smith's conclusion is incumbered with the further absurdity that agriculture in new colonies does not create rent and does not keep three people, though of course it is just as good for the public there as in old countries.

Although, therefore, Adam Smith had the merit of teaching the world that the exchangeable value of commodities is proportioned to the cost of their production, his analysis of that cost was so very defective as to throw that part of political economy into great confusion for many years, and as quite to prevent his teaching being used as an authority upon it now.

The causes which regulate the value of securities, whether debts or shares, Adam Smith did not attempt to investigate at all; and it was not to be expected that he should do so, for such things were in his day a very unimportant part of wealth compared with that which they are now. And if, as we have seen, Adam Smith's conception of "average" value and of the causes producing it was then imperfect, his idea of monetary or market value was much worse. He says:—

"The actual price at which any commodity is commonly sold is called its 'market price'; it may either be above or below or exactly the same with its natural price.

"The market price of every particular commodity is regulated by the proportion between the quantity which is actually brought to market, *and the demand of those who are willing to pay the natural price of the commodity*, or the whole value of the rent, labor, and profit which must be paid in order to bring it thither. Such people may be called the 'effectual demanders,' and their demand the 'effectual demand'; since it may be sufficient to effectuate the bringing of the commodity to market. It is different

from the absolute demand: a very poor man may be said in some sense to have a demand for a coach and six, — he might like to have it; but his demand is not an effectual demand, as the commodity can never be brought to market in order to satisfy it." *

But the actual price at which a thing is sold, is determined not solely by the demands of those who are willing to pay the average price of the commodity, but by everybody's demand who bids for it. It is, as we have seen, an exchange determined by the quantity of the commodity in the market and the desires of its holders, as compared with the quantity of money in that market and the desires of its holders; it is a case of barter determined by relative quantities and relative feelings. And the phrase "effectual demand," if defined to mean the demand of those willing to pay cost price, is misleading; because the money offered by those willing to pay cost price is not sufficient to be effectual when articles are particularly in demand, and therefore sell for more than it cost to make them, and is more than sufficient to be effectual when the demand for articles is particularly slack, and when therefore they sell for less than it cost to make them. The whole idea is confused.

In other passages, Adam Smith takes a view far better than in this: but this is the place where he ought to have taken the best, for it is the guiding paragraph of his special disquisition upon the subject; and his being not so good upon it here as elsewhere shows that his elementary conception was defective in definiteness. And nothing is more natural than that it should be so. Perhaps, as I have said before, Adam Smith's mind was by nature rather disinclined to an anxious accuracy in abstract ideas; and a century of critics on these facts and these times have sharpened our perception since he wrote on them. We must not expect from him the use of modern

* Book i., Chap. vii. (Italics Bagehot's.)

"words of precision," any more than we should find fault with a marksman of his generation for not using a rifle: neither such "arms of precision" nor such "words of precision" then existed. And there was then little encouragement to think out the subject: Adam Smith evidently hurries over the abstract part of it because he thinks his readers will not attend to it. Even now, a writer who wishes to be read beyond a very narrow circle must be careful not to be too elaborate; and in the last century the case was certainly far worse. Many great writers — Montesquieu and Hume especially — would have written far more instructively, and as we should now think, far better, if they could have relied on any careful attention from their readers; they evidently thought that their writings would be principally read by persons who would cease to read as soon as they became dull. Nowadays the diffusion of physical science — even of popular physical science — has partly taught us that much truth is dull and complex, and that the most interesting parts of truth can only be understood by those who have mastered that dull and complex part; but even now we do not remember this half enough.

After these specimens, it would evidently be tedious to criticize the "Wealth of Nations" as if it were a treatise of modern political economy. We have given some account of what would be its answer to the first question of that science, "What makes all things exchange for more or less of other things?" and we see from it what the answer to other similar questions would be like. Nothing could be more unjust to a great writer than to judge of him by a standard which he did not expect, and to blame his best book for not being what he never thought of making it; especially when, except for him, we should never have imagined the standard, or conceived the possibility of the book being that which we now blame it for not being. We might

as well expect that the first cultivators of a country should make the best permanent road, as that the first propounders of great conceptions should shape them into the finished form most useful to posterity.

The ways really to appreciate Adam Smith are two.

First, you should form a clear notion of the state of the received political economy of the world at the time he wrote. The last treatise on the subject published in England before the "Wealth of Nations" was "The Principles of Political Economy," by Sir James Steuart. The author was a man of culture and travel, acquainted with a great variety of economical facts, and conversant with what had been written before upon the subject; he was a man of considerable natural ability, respected and consulted in his time; and his book is still worth looking over, for it contains many facts and reasonings which are curious: and this is the sort of thing he writes:—

Much foreign trade he considers mischievous. He propounds a plan—a foreign trade that is really desirable for a nation—founded on the three following "easy principles":—

"The first,—That in a country entirely taken up with the object of foreign trade, no competition should be allowed to come from abroad for articles of the first necessity, and principally for food, so as to raise prices beyond a certain standard.

"The second,—That no domestic competition should be encouraged upon articles of superfluity, so as to raise prices beyond a certain standard.

"The third,—That when these standards cannot be preserved, and that from natural causes, prices get above them, public money must be thrown into the scale to bring prices to the level of those of exportation.

"The greater the extent of foreign trade in any nation is, the lower these standards *must* be kept; the less the extent of it is, the higher they may be allowed to rise."*

And taking the subject more practically, he says, "It is . . . a general maxim, to discourage the importation of work and to

* Book ii., Chap. xv.

encourage the exportation of it;"* and upon that footing he asks and discusses, "What is the proper method to put a stop to a foreign trade in manufactures when the balance of it turns against a nation?"†

This is the kind of authoritative doctrine which ruled in Adam Smith's time, and from which he delivered us.

The second way is, to take up Adam Smith himself and read him. There are scarcely five consecutive pages in the "Wealth of Nations" which do not contain some sound and solid observation, important in practice and replete with common-sense. The most experienced men of business would have been proud of such a fund of just maxims fresh from the life; and it is wonderful that they should have occurred to an absent student, apparently buried in books and busy with abstractions. Most of such students, so far from being able to make such remarks, would not comprehend their value; would acknowledge that they could not see much in them if they were elaborately explained to them. Adam Smith himself probably did not know their exceeding merit, and preferred more learned parts of his writings, which are now obsolete, and more refined parts, which are now seen to have little value. Lord Bacon says of some one that he was "like Saul, who went in search of his father's asses and found a kingdom;"‡ and this is exactly what happened to Adam Smith. He was engaged in a scheme of vast research, far surpassing the means at his disposal, and too good§ for any single man. In the course of that great pursuit, and as a small part of it, he came upon the "Wealth of Nations," for dealing with which his powers and his opportunities peculiarly fitted him; and on that he wrote a book which has itself

* Book ii., Chap. xxiv.

† Title of above chapter.

‡ I find no such simile in Bacon's works or letters. — Ed.

§ Probably a misprint for "grand." — Ed.

deeply influenced thought and policy, and which has been the beginning of a new science. He has obtained great fame, though it was not that fame which was the dream of his life; for

> "What was before us we know not,
> And we know not what shall succeed."*

*Matthew Arnold, "The Future."

MALTHUS.

THE next great advance in political economy was made almost in as unlikely a manner. In the middle of the last century there lived in the South of England a certain Mr. Daniel Malthus, who was a "friend and correspondent of Rousseau, and one of his executors."* This gentleman had adopted all Rousseau's ideas of the perfectibility of man, and of the speed with which he would improve if he were only left to himself and set free from the chains of ancient custom; the air of that time was full of such ideas, and many otherwise quiet and rational persons were excited and enthusiastic about them. Mr. Daniel Malthus had a clever son, Robert, whom he educated with great care, and to whom, doubtless, in season and out of season, he communicated his favorite ideas; at any rate, Robert grew up with a proper antipathy to them. The instructive reaction of child against parent, which more than almost anything keeps men moving, and prevents "one good custom" from "corrupting the world," has seldom had a better example. "Train a child up in the way he should go," a cynic has observed, "and then you may feel safe that he will not walk in it:" let a child hear much from infancy of nice dreams and pleasing visions, and to the best of your ability you will have prepared him for prosaic carefulness and a dismal rationalism.

"The 'Essay on The Principle of Population,'" says Mr. Malthus, "which I published in 1798, was suggested, as is expressed in the preface, by a paper in Mr. Godwin's 'Inquirer';"† and there is a curious

* Memoir prefixed to second edition of Malthus's "Principles of Political Economy" (1836).

† Preface to second edition of the Essay.

story about it. Mr. Godwin was a disciple of Rousseau, and had drawn up a plan of village perfection, in which "every rood was to maintain" its man, and in which mankind were to be happy and at ease, without the annoying restraints of property and marriage. Such "elysiums" have been sketched in all ages, and there is nothing remarkable about them; but Mr. Malthus's reply was very remarkable.

"You may," he said, "imagine this perfect picture for a little while, but it will not last; it cannot last: Nature is against it. She has a principle — that of population — which is sure to destroy it. Mankind always, by her arrangements, increase as fast as they can; misery checks their increase, and vice checks it, but nothing else. A perfectly happy and virtuous community, by physical law, is constrained to increase very rapidly; if you look into the fact you will find that it will double every twenty-five years: but there can be no similar increase in their food. The best lands are taken up first, then the next best, then the inferior, at last the worst; at each stage the amount of food produced is less than before. By nature, human food increases in a slow arithmetical ratio; man himself increases in a quick geometrical ratio, unless want and vice stop him: so that if you make him happy in a village community for a moment, he will soon multiply so that he shall cease to be happy; there is nothing to stop him; he will ere long reach the inevitable limit where want and wickedness begin to keep him down."*

The world rather eagerly read this doctrine, for the reaction against dreams and visions was strong in many minds. The event of the French revolution had upset all calculation, broken up all pleasing visions, and disheartened half — or indeed much more than half — mankind. Mr. Malthus was as much the mouth-piece of his generation in exposing Utopias as his father had been in accepting them; the "Essay on Population" in its first edition was read with eager avidity, and its doctrines seem to have been much believed.

Still, when examined, the tenets seemed startling; and what made them even more surprising was that

* This is of course an imaginary summary, not an exact quotation. — Ed.

their propounder, Mr. Malthus, was a clergyman. People objected, "Can this really be so? Is it consistent with religion? Can we believe that inevitably man is yoked to sin and misery? that even if you make him good, and if goodness makes him happy, the structure of earth and nature is such as inevitably in a few years to make him miserable again? How is this possible under a benevolent Creator? How can it be made to accord with revelation?" Such objections were difficult to answer, especially as Mr. Malthus was a simple candid man, and they seem to have had much effect in changing his views; at least, in the Preface to the second edition, he tells us, "Throughout the whole of the present work, I have so far differed in principle from the former as to suppose the action of another check to population, which does not come under the head either of vice or misery." This is the celebrated principle of "self-restraint, moral or prudential." And he goes on to say that he has "endeavored to soften some of the harshest conclusions of the first essay;" but he does not seem to see that he has cut away the ground of his whole argument. If there be this principle of virtuous self-restraint, he no longer answers Godwin; he no longer destroys the dreams of perfectibility. If it be possible for a perfectly virtuous community to limit their numbers, they will perform that duty just as they perform all others: there is no infallible principle that will break up the village community; it can adjust its numbers to its food, and may last forever. In its first form the "Essay on Population" was conclusive as an argument, only it was based on untrue facts; in its second form it was based on true facts, but it was inconclusive as an argument.

From this unlucky beginning the established doctrine in political economy of "Population" is to be dated; and as was not unnatural, so odd a commencement was unfavorable to its comprehension. From the mode in which he first regarded the subject,

it was natural that Mr. Malthus should think more of the painful aspects of the subject than of the opposite ones. At first there were no cheerful aspects,—the doctrine was an apparatus for destroying cheerfulness; in its second and truer form it is far less painful, though like most great truths about the world (especially economical ones, which have so much to do with labor and toil), it has its painful side. But Mr. Malthus first put the painful side alone forward, fixed the public mind upon it, and for many years it could see no other.

There is much in the theory of population which it would require a large book to discuss, and I am far from pretending that I could write that book. Many most difficult questions of morals, and many others of physiology, must be treated of; and it is especially hard to discuss such questions *virginibus puerisque*, as almost all questions are now discussed,—some parts of it could scarcely be managed except under the decent veil of a dead language.* The conditions of marriage form only part of that subject, and a great deal would have to be written on that part in its relations to the actual past and to the possible future; but what is necessary for abstract political economy is much easier. As has been explained in the introduction, the peculiarity of this science is, that it abstracts—that is, it seizes upon and alone considers—the principal peculiarities of existing man as we find him in the principal commercial nations. It does not profess to be accurately complete as to those nations even as they are now, still less as they once were or as they may hereafter be; and still less again does it pretend to be true of other nations, in ages of a different character, cast in a different mold, and occupied with different ideas. Human nature is so various that we cannot treat of it at once briefly and fully; we can only reason on short propositions, and therefore we must

* "The obscurity of a learned language."—Gibbon, Autobiography.

cut the subject up into distinct portions, each of which can be conceived of by itself and heard out by itself: and no part of human nature is more infinite than the relation between the sexes, and its consequences.

Mr. Malthus had no idea of looking at the subject in this way; he thought he was dealing with all nations and all ages. In its original form the "Essay" propounded a universal principle, destructive of golden visions; in its later forms he deals first with principles of population in the most barbarous ages, and then with it in every variety of society which he knew of, — nomad or stationary, commercial or agricultural: and there is much in his discussion of the savage society which is still worth reading, and which was much before his time. His mind was by nature indisposed for and unfit for abstractions; indeed, if I may say so with reverence, he always seems to me but a poor hand at a dry argument. Like Adam Smith, he had no idea that he was founding an abstract science, — he thought he was dealing wholly with the concrete world; but it so happened that his idea of the concrete world coincided with the most convenient abstraction that can be made from it, and so he became in spite of himself the founder of an abstract science.

The assumed laws of population in abstract political economy are these: —

First. That population would soon outstrip the means of feeding it, if it were not kept down by vice, misery, or self-restraint.

Secondly. That in a state of society where self-restraint does not act at all, or only acts so little that we need not think of it, population will augment till the poorest class of the community have only just enough to support life.

Thirdly. That in a community where self-restraint acts effectually, each class of the community will augment till it reaches the point at which it begins to exercise that restraint.

In the second case (which was all that Malthus thought of in his first edition), the population increases till it reaches a physical minimum of subsistence, — one that is set by natural causes; in the other it increases till it reaches a moral minimum of subsistence, — that is, one set by human choice. And it follows that in improving communities this moral minimum is commonly rising; for in most communities more self-restraint of this sort is desirable, and as people improve they mostly are more inclined to exercise it. The physical minimum must be a fixed minimum; the moral may be, and ordinarily is, a moving minimum. A political economist does not imagine (as I have previously explained) that vice, misery, and self-restraint are the only causes which affect the rate of increase of population; he well knows that many others act on it: all he says is, that in the principal commercial communities of the world these causes are now in most powerful operation, though they are retarded or helped by others; in a word, that these selected causes will in such communities produce the specified results, in more or less time, though there are other causes which aid in settling how long or how short that time is to be.

For example, it might well be (though I do not know that it has been proved) that some races of men from inherent organization tend to augment faster than other races. The causes which divide men into races are so many [and] so hidden, and produce so many effects, that it would not be strange if they had this effect among others; perhaps there would be more *a priori* likelihood that they would have such an effect as this than that they would produce some actual effects which are quite certain. There is much evidence that different climates affect differently the sexual desires, some aggravating them and some calming them; and it would seem likely that those races which had in this respect for

ages been exposed to intensifying influences, would augment more rapidly than those which had been exposed to mitigating ones. Our knowledge of race-making causes is still most imperfect, and we can never trace race effects separately; they are always combined with the effects of many other causes. In this case the confusion is peculiarly complex, for rules of morality — arising in unknown circumstances and inherited for untold ages — so retard or quicken the growth of population that it is impossible to isolate the purely physiological phenomenon. Still, the principles above laid down afford all possible room for it; they will have their usual action, though morality will have a concurrent action.

Secondly, we may quite believe that the nervous conditions which luxury engenders are less favorable to the prolificness of population than simpler conditions. On this point (and on this point only) of the theory of population, Adam Smith had remarkable and sound views: "A half-starved Highland woman," he tells us, "frequently bears more than twenty children; while a pampered fine lady is often incapable of bearing any, and is generally exhausted by two or three. Barrenness, so frequent among women of fashion, is very rare among those of inferior station."* Probably of all causes which regulate the pace of population, the nervous state of the woman is the most important; and it seems to have a kind of cyclical course as society advances. There is much reason to think that in the earliest state in which we know men to have lived, — the state of the old slave age and the present savages, — the hard labor and insufficient food of the woman tend very much to keep down the increase of numbers; at a later period the improvement of food, better shelter, diminution of work during pregnancy, bring the bearing power of women up to its maximum, — the Highland woman of Adam Smith probably was

* Book i., Chap. viii.

able to bring into the world as many children, and (physically at least) as strong children as any one who ever lived. After that, not only the luxury of which he speaks, but education and the habit of using the mind, tend almost certainly to diminish the producing power: there is only a certain quantity of force in the female frame, and if that force is invested, so to say, in one way, it cannot be used in another.

The same force acts, no doubt, on man, but probably differently. The use of the mind in some ways certainly does not have much if any effect on the power of increasing the race, — the English judges whose children Mr. Galton counted, showed very considerable capacity of this sort, and they worked in their way as hard as many people ever have or will; but for the most part they do their work with a joyous swing and impetus which show that it does not tell upon the nerves. But anxiety, as has been said, does so tell, and we have seen that there is reason to believe that it much tends to slacken the growth of population; and probably any of the higher exercises of the mind, which cause as they all do obscure and subtle pain, have a similar effect. But these are problems for the future: no one can say that they are solved as yet; indeed, we are only beginning to try to solve them. Some have been sanguine enough to fancy that the accumulation of them may in distant ages make a stationary state possible, and make it pleasant; but with this, political economy has nothing to do. It deals with men here and now; it takes certain parts of their nature which are indisputable and which are important, and considers how these would operate by themselves: questions as to the ultimate effects of other agencies, physiological or mental, it leaves to other sciences and to futurity.

In the same way, then, political economy cannot by itself pretend to solve the many new problems

which the sanitary condition of great cities suggests in this age of them. There can be little doubt that these great accumulations of human beings have at least three effects.

First, Mr. Galton holds that they diminish in some unknown degree the number of births.

"Again, there is a constant tendency of the best men in the country to settle in the great cities, where marriages are less prolific and children are less likely to live. Owing to these several causes, there is a steady check in an old civilization upon the fertility of the abler classes; the improvident and unambitious are those who chiefly keep up the breed. So the race gradually deteriorates, becoming in each successive generation less fitted for a high civilization, although it retains the external appearances of one, until the time comes when the whole political and social fabric caves in, and a greater or less relapse to barbarism takes place, during the reign of which the race is perhaps able to recover its tone." *

And these consequences seem to Mr. Galton purely evil; but they do not seem so to me. No doubt it is an evil that the accumulation of men in cities weakens the frame, and that they have not the same energy or health as those in the country; every one must regret this decline of power: but when power has declined in a certain race, it is better that that race should not increase as fast as others, — we had better breed from hardy than from weakened specimens. The diminished growth of urban populations seems to be nature's remedy for the diminution in their strength.

Secondly, great towns indisputably encourage drunkenness. The bad state of the atmosphere there certainly inclines men more to drink than the better air of the country, and this is no doubt a great evil; but we may doubt if it is an evil without compensation, — the persons most inclined to drunkenness are generally persons of some nervous taint or weakness which they often inherited themselves, and

* "Hereditary Genius," page 362.

which they might not improbably transmit to their children. I do not of course mean that this inherent weakness is irresistible: no doubt the mass of these people can (at first, at least) help drinking very well, — the heritable taint amounts only to an increased liability to this temptation; but this is quite reason enough to wish that it should not be inherited. Great cities seem to have this special function in the world, that they bring out this taint in the worst specimens; not only do such persons suffer as usual from the general decline in the multiplying power of city populations, but they also suffer in a way peculiar to themselves. One of the effects of a drunken habit is to diminish this kind of power as well as, and perhaps more than, most others.

Thirdly, great cities collect together a great criminal population, and make them sterile; and so far as crime is connected with a low type of nervous organization, as it is very often, this sterility is a great gain, — society gets rid of these over-tempted persons, whose peculiar defects are a danger to others as well as to themselves. Great cities must always be in their worst aspects painful spectacles; but this painfulness is somewhat relieved when we see that we can regard them as a huge cleansing machinery, which no doubt shows us a great deal that is detestable, but also takes away much of it, and prevents more coming, not only in that place but in others.

Nor has political economy any concern with the other purging means, which in a subtle way nature seems to use all through civilized society. It is said that man is the only animal of whose breed no care is taken; but nature has not forgotten to take much care of it. Every one who watches society must have seen many instances in which defective families have died out because they were defective: the men being weak failed to earn their living, and therefore could not marry; and the girls, wanting from the same cause life and vigor, did not find husbands, — and so

the race died away. And this cause works not only in families weak as a whole, but in the weak members of strong families; all through society there is a constant tendency in civilized life to slacken the pace of population by weeding away those weaker and less valuable.

There seem to be curious processes of nature also at the other end of the scale of cultivation. The process by which so many savage races die out before civilized man is certainly not as yet completely explained. Hard work, which civilized man brings, and which most savages cannot bear, accounts for some of it; alcohol — "the fire-water," as savages call it — accounts for more: but there seems to be a residue still unexplained. The most plausible theory says that this is due to two causes; and first, to the inability of savage nations to bear the diseases to which the hardened frame of civilized men is inured. For ages, in the contested parts of the world which civilized man inhabits, the stronger race has conquered and supplanted the weaker; and the result is a strong animal, equal to many difficulties, and able among other things to survive strong diseases: but in the out-of-the-way places which savages inhabit there has been no such incessant conflict, and in consequence there is no such strong animal, — the weaker savage succumbs to diseases which the seasoned white man easily bears. Indeed, the way in which savages waste away before "alcohol" is but a case of this: they cannot bear, as white men can, the diseases which it generates. And the second cause which co-operates with this is a certain disheartened tendency of mind which somehow tells on the nerves, and which is analogous to the way in which wild animals die out when caught and confined; a certain life and spirit seem as essential to keep men in good numbers as in good health.

Different kinds of food may, too, for aught we know, have an effect not yet understood on man's

power to increase his numbers. The potato was at one time fancied — erroneously, probably — to contain a particular stimulus of this sort; but though this instance may have been a mistake, the conception is possible. We must not always say, [however,] that the more nutritious food will tend universally to produce the more people, though no doubt it usually does so: it may even sometimes have a contrary effect, — it may run to quality rather than to quantity; it may make fewer strong people instead of more weak ones.

I set out these considerations at length because it is most important that there should be no disunion between political economy and physiology, or between it and the more complex forms of social science. No political economist has the slightest reason to depreciate the causes which act on population of which his science takes no cognizance: on the contrary, he has the greatest reason for taking an interest in them, — they supplement what he discusses; reality is composed of the influences treated of in his science, *plus* these influences, and of course he wishes to compare his work with fact.

We must be careful to see what these principles themselves mean; for they are often mistaken. Even apart from physiology, they do not say that an increase in the comfort of a people necessarily tends to augment their numbers; it does so in two cases only. The first case is when the people are at the "physical minimum," with just enough to support life, and do not exercise self-restraint; here, the moment there is more food there will be more numbers. Such people will always multiply, just as the ryots in Bengal, in a somewhat similar state of things, are multiplying. The second case is when the people are at the "moral minimum," with just what will support the existing numbers in the sort of life they think proper, be it high or low; such numbers being kept down by self-restraint, and when the people do not

change their standard. Then, undoubtedly, more comfort will be turned into more children ; and in a little while the new state of things will produce no more comfort to each person than the old one, only there will be more persons to enjoy it. But there is no sort of necessity in this ; as has been explained, the "moral minimum" is very movable : the people may change their standard, and in that case more comfort will not produce more persons, — there will only be as many as there would have been before, and the average of these will have a better life. Whether a people take one course or the other will depend on this sort of change, and on its relation to the sort of civilization enjoyed by the people ; I doubt if any general formula can be found for it. Some writers have said that a great sudden change which elevates a whole generation is more likely to raise the population standard than a series of successive small changes ;* but as far as I can judge, more depends on the previous preparation of the people than on its absolute amount. A really thrifty people used to self-denial will profit exceedingly by a series of small improvements, — they will not "run to numbers," they will augment in happiness ; and an easy-going enjoying nation will mostly not be much the better for any boon of plenty, however great or sudden, — they will live at the same average, but the average will not be raised.

Now that we see the extreme delicacy of the assumptions as to population on which abstract political economy is based, we shall not be surprised at finding that Mr. Malthus did not apprehend them as they really are. As I have said, he did not in the least know that he was aiding in the foundation of an abstract science ; he thought that he was dealing with real men, and that the principles which he expounded were all those which affected his subject.

* It is not hard to prove that the fact is quite as likely to be just the reverse. — Ed.

Indeed, the best part of his book is an account, which must have cost great labor at that time, of the rate at which population had augmented and was augmenting, in various countries, and the causes which influenced that rate: and the best part of this is that which relates to the savage state; for even now, when that state has been so accurately studied, it is worth while to glance over what Malthus wrote on it more than fifty years ago. That his analysis of population causes in other countries should be most incomplete was a matter of course, — even now we are much in the dark on much of this subject; but how incomplete it was, will sufficiently appear from a single fact: though he treats elaborately of Norway and of Switzerland, he has no idea that peasant properties have a tendency to check population. He discusses the subject as if there were no difference in this respect between a people which owns the soil and one which lives by wages; and therefore many of the disquisitions in which he indulges are wholly thrown away.

And Mr. Malthus, as was natural, never cleared his mind entirely of the dismal theory with which he began. Scarcely any man who has evolved a striking and original conception of a subject ever gets rid of it; long after he himself fancies that he has cleared his mind of it, every one else sees that it haunts him still. Mr. Malthus was peculiarly little likely to get rid of his errors: he had published his original theory, had made a name by publishing it, and he never admitted even to himself how complete a change the foundation of his ideas had undergone. A theory of population which does not include self-restraint, like his first, and one which essentially depends on it, like his second, differ in their essence and therefore differ in their main consequences. From a theory of population which does not include a prudential check, it follows that plenty cannot last, and that men will always multiply down to misery;

but such a theory with a prudential check has no such consequence: and for many years it was a misfortune to the subject that the original propounder of what were then the best views of it had connected those views with a mischievous exaggeration, leading straight to lamentable results.

To most other parts of political economy Mr. Malthus added very little; and on some he supported errors which were even then becoming antiquated. He was a strenuous advocate of "Protection to agriculture," and believed that the supply of all commodities might exceed the demand, which is as much as to say that there is too much of everything. The truth is, that Mr. Malthus had not the practical sagacity necessary for the treatment of political economy in a concrete way, or the mastery of abstract ideas necessary to deal with it in what we should now call a "scientific" way; he tried a bad mixture of both, — there is a mist of speculation over his facts and a vapor of fact over his ideas.

On one important point Mr. Malthus was, however, in advance of his time, — he was one of several writers who at the same time discovered the true theory of rent; that theory lay indeed close to his ideas on population. Its essence (as we have seen) is, that the rent of land arises from the scarcity of good land. Mr. Malthus could not help seeing that Adam Smith (and the French *économistes*) were wrong in imputing rent to some pre-eminent merit in the land: he saw that it came from a special fact concerning land, — viz., that so little of it is first-rate both in situation and in quality; that most is either not the best or not in the best place, else there would be no rent of land any more than of air. This truth seems so plain that one can scarcely conceive how it should ever not have been seen; but certainly it was not seen till modern economists pointed it out; and then — as so often happens — it was on many people's lips almost at once. The fact

was so unmistakably plain that several persons could not help seeing it the moment they began to search for it. Of these, Mr. Malthus was one, but not the best; as we shall see, a much keener intellect than his far more fully examined all its consequences.

There is nothing in Mr. Malthus's life which is worth mentioning, or which illustrated his doctrines. He was an estimable gentleman and clerical professor; "a mild pottering person," I think, Carlyle would have called him. Neither his occupation nor his turn of mind particularly fitted him to write on money matters: he was not a man of business, nor had he, like Paley and similar clergymen, a hard-headed liking for and an innate insight into the theory of business. He was a sensible man educated in the midst of illusions; he felt a reaction against them, and devoted the vigor of his youth to disprove and dispel them: and he made many sensible and acute remarks on kindred topics. But he has been among the luckiest of authors, for he has connected his name with the foundation of a lasting science which he did not plan and would by no means have agreed in.

This celebrity may seem over-fortunate, but it is explained by the circumstances of the time: the age in which he wrote was as much against the Godwinian illusions as Mr. Malthus could be. He and his father were but an instance of a general contrast between successive generations: the generation before 1789 was full of hope, and delighted with happy schemes; that after it was terrified by the French revolution, insensible to hope and ready for despair. To this change of sentiment Mr. Malthus effectually ministered; and beneath this want of the surface there was one much more real need, to which he was of use also, — an immense tide of sentiment favored the growth of population, no matter what the circumstances and what its means of subsistence. Mr. Pitt, who was the most instructed statesman of

the time on economical subjects, said that the man who had a large family was "a benefactor to his country": and the old English Poor Law was simply a subsidy to the increase of paupers. Against such notions and such practices Mr. Malthus's views were a most admirable reaction; if there had been no such movement, our agricultural districts would by this time have been a pauper warren. That his views were exaggerated, though a subsequent misfortune, was an immediate advantage: he advertised his notions, and fixed them among the men who understood a simple and striking exaggeration far more easily than a full and accurate truth. He created an entirely new feeling on his subject.

"If we look," says Mr. Carlyle, "at the old Poor Law, we shall find it to have become still more unsupportable; demanding, if England was not destined for anarchy, to be done away with." "To create men filled with a theory" that it ought to be done away with "was the one thing needful; nature had no readier way of getting" it done away with.* To this Mr. Malthus most essentially contributed; it was he who more than any one else "filled" men with that theory.

*"Chartism," Chap. iii.

RICARDO.

THE true founder of abstract political economy is Ricardo; and yet in seeming there was no one less likely to be the founder, — he was a practical man of business, who had little education, who was for much of his life closely occupied in a singularly absorbing trade, and who made a fortune in that trade. Just as no one would have expected from Adam Smith, the bookish student, the practical sagacity with which every page of the "Wealth of Nations" overflows, so no one would have expected from Ricardo, who made a large fortune, the foundation of a science of abstractions; every one would, on the contrary, have imagined that Adam Smith would have been eminent in the abstractions among which his closet-life would seem to have been spent, and that Ricardo would have been eminent in the rough and rude sense which makes money: but in fact, Ricardo arrives at his best conclusions by the most delicate and often difficult reasoning, and Adam Smith, as we have seen, at his by an easy and homely sagacity.

There is much in this, as in all such cases, which now is and probably will always remain inexplicable; for the most obscure and subtle of causes are those which fix inherited genius. But just as in Adam Smith's case, a more exact survey of the circumstances tends to diminish our surprise: the trade in which Ricardo spent his life, and in which he was so successful, was of all trades the most abstract. Perhaps some people may smile when they hear that his money was made on the Stock Exchange, which

they believe to be a scene of gambling; but there is no place where the calculations are so fine, or where they are employed on data so impalpable and so little "immersed in matter."* There is a story that some dealer made very many thousand pounds by continued dealings in the shares of some railway, and then on a sudden asked where that railway was: the whole thing had been a series of algebraic quantities to him, which called up no picture, but which affected a profit-and-loss account. In most kinds of business there is an appeal of some sort to the senses: there are goods in ships, or machines; even in banking there is much physical money to be counted: but the Stock Exchange deals in the "debts"—that is, the "promises"—of nations, and in the "shares" of undertakings whose value depends on certain future dividends,—that is, on certain expectations, and what those expectations are to be is a matter of nice calculation from the past. These imponderable elements of trade cannot be seen or handled, and the dealing with them trains the mind to a refinement analogous to that of the metaphysician. The ordinary human mind finds a great rest in fixing itself on a concrete object: but neither the metaphysician nor the stock-jobber have any such means of repose; both must make their minds ache by fixing them intently on what they can never see, and by working out all its important qualities and quantities. A stock-jobber loses money, and in the end is ruined, if he omits any or miscalculates any; if any man of business is to turn abstract thinker, this is the one who should do so. Any careful reader of Ricardo, who knows anything of such matters, and who watches the anxious penetration with which he follows out rarefied minutiæ, will very often say to himself, "I see well why this man made a fortune on the Stock Exchange."

For this trade Ricardo had the best of all preparations, the preparation of race: he was a Jew by

* "Locke on the Human Understanding," Book iv., Chap. iii., § 6.

descent (his father was one by religion), and for ages the Jews have shown a marked excellence in what may be called the "commerce of imperceptibles." They have no particular superiority in the ordinary branches of trade; an Englishman is quite their equal in dealing with ordinary merchandise, in machine making or manufacturing: but the Jews excel on every Bourse in Europe; they — and Christian descendants of their blood — have a pre-eminence there wholly out of proportion to their numbers or even to their wealth. Some part of that pre-eminence is no doubt owing to their peculiar position as a race: for nearly two thousand years they have been a small nation diffused over a vast area; that diffusion has made them the money-lenders for most of the nations with whom they lived; and the exchange of money between country and country is a business of fine calculation, which prepared them for other fine calculations. This long experience has probably developed a natural aptitude, and it would be idle to distinguish what is due to the one in comparison with the other; the fact remains that the Jews have now an inborn facility in applying figures to pure money matters. They want, less than other nations, a visible commodity which they can imagine if not touch; they follow with greater ease and greater nicety all the minute fractions on which this subtle commerce depends (a task which is a particular torture to most Englishmen), and they make money as the result. The writings of Ricardo are unique in literature, so far as I know, as a representative on paper of the special faculties by which the Jews have grown rich for ages. The works of Spinoza and many others have shown the power of the race in dealing with other kinds of abstraction; but I know none but Ricardo's which can awaken a book student to a sense of the Jewish genius for the mathematics of money-dealing. His mastery over the abstractions of political economy is of a kind almost exactly identical.

The peculiar circumstances of his time also conducted Ricardo to the task for which his mind was most fit. He did not go to political economy; political economy, so to say, came to him. He lived in the "City" at a time when there was an incessant economical discussion there: he was born in 1772, and had been some years in business in 1797, the year of the celebrated "Bank restriction," which "restricted" the Bank of England from paying its notes in coin, and which established for the next twenty years in England an inconvertible paper currency. As to this — as to the nature of its effect, and even as to whether it had an effect — there was an enormous amount of controversy; Ricardo could not have helped hearing of it, and after some years took an eager part in it. Probably if he had not been led in this way to write pamphlets, he would never have written anything at all, or have got the habit of consecutive dealing with difficult topics, which is rarely gained without writing, — he had only a common-school education, and no special training in such things; but it is the nature of an inconvertible currency to throw the dealings between other countries and the country which has it into confusion, and to change the price of all its securities. As Ricardo was a jobber on the English Stock Exchange for the whole time during which the notes of the Bank of England were inconvertible, his daily business must have constantly felt the effect.

Having been thus stimulated to write pamphlets on the one great economical subject of his day, Ricardo was naturally led to write them also on the other great one. At the close of the war the English Parliament was afraid that corn would be too cheap: the war had made it dear, and probably when peace came it would cease to be dear; and therefore in its wisdom Parliament passed "Corn Laws" to keep it dear. And it would have been difficult for a keen arguer and clear thinker like Ricardo to abstain from

proving that Parliament was wrong; and accordingly he wrote some essays which would be called "dry and difficult" now, but which were then read very extensively and had much influence.

Political economy was indeed the favorite subject in England from about 1810 to about 1840, and this to an extent which the present generation can scarcely comprehend. Indeed, old people are puzzled for an opposite reason: they can hardly understand the comparative disappearance of what was the principal topic in their youth. They mutter with extreme surprise, "We hardly hear anything now about political economy: we used to hear of nothing so much." And the fundamental cause is the great improvement in the condition of the country. For the thirty years succeeding the peace of 1815, England was always uncomfortable: trade was bad, employment scarce, and all our industry depressed, fluctuating, and out of heart. So great is the change of times, that what we now call "bad trade" would then have seemed very good trade, and what we now call "good trade" would have been too good to be thought of, — would have been deemed an inconceivable Elysian and Utopian dream. So long as this misery and discomfort continued, there was a natural curiosity as to the remedy; business being bad, there was a great interest in the "science of business," which ought to explain why it was thus bad and might be able to show how it was to be made good. While the economical condition of countries is bad, men care for political economy, which may tell us how it is to be improved; when that condition is improved, political economy ceases to have the same popular interest, for it can no longer prescribe anything which helps the people's life. In no age of England, either before or since, could a practical man of business like Ricardo have had so many and such strong influences combining to lead him towards political economy, as in Ricardo's own time.

And there was at that time a philosophical fashion which was peculiarly adapted to make him think that the abstract mode of treating the subject which was most suitable to his genius was the right mode. It was the age of "philosophical Radicalism,"—a school of philosophy which held that the whole theory of political government could be deduced from a few simple axioms of human nature; it assumed certain maxims as to every one's interest, and as to every one always following his interest, and from thence deduced the universal superiority of one particular form of government over all others. "Euclid" was its one type of scientific thought; and it believed that type to be—if not always, at least very often—attainable. From a short series of axioms and definitions it believed that a large part of human things—far more than is really possible—could be deduced. The most known to posterity of this school (and probably its founder) was Mr. Bentham, for the special value of his works on jurisprudence has caused his name to survive the general mode of political thinking which he was so powerful in introducing; but a member of the sect almost equally influential in his own time was Mr. James Mill, of whom his son has given us such a graphic picture in his biography. This austere dogmatist thought that the laws of government and of human happiness might be evolved from some few principles, just as a Calvinistic theologian evolves a whole creed of human salvation from certain others. Mr. Grote, who belonged for the best years of his life to the sect, and whose writings and tone of mind were profoundly tinctured by its teaching, has left us a vivid description of Mr. James Mill, who seems to have influenced him far more than any one else; and an equally vivid picture may still be found in the reminiscences of a few old men, who still linger in London society, and who are fond of recalling the doctrines of their youth, though probably they now

no longer believe them. James Mill must have pre-eminently possessed the Socratic gift of instantaneously exciting and permanently impressing the minds of those around him.

I do not know in what manner Ricardo and James Mill became acquainted, except that John Mill says it was through Bentham, who was a rich man, and though a recluse, made for many years his house a sort of castle. John Mill tells us also that James Mill considered the friendship of Ricardo to have been the most valuable of his whole life. To a genius like Ricardo, with Ricardo's time and circumstances, the doctrines of James Mill must have come like fire to fuel; they must have stimulated the innate desire to deduce in systematic connection, from the fewest possible principles, the truths which he had long been considering disconnectedly. If Ricardo had never seen James Mill, he would probably have written many special pamphlets of great value on passing economical problems, but he would probably not have written "On the Principles of Political Economy and Taxation," and thus founded an abstract science; it takes a great effort to breathe for long together the "thin air" of abstract reasoning.

It must be remembered that Ricardo was in no high sense an educated man. As far as we know, he had not studied any science, and had no large notion of what science was; without encouragement from a better trained mind he most likely would not have attempted any purely scientific effort. To the end of his days, indeed, he never comprehended what he was doing. He dealt with abstractions without knowing that they were such; he thoroughly believed that he was dealing with real things. He thought that he was considering actual human nature in its actual circumstances, when he was really considering a fictitious nature in fictitious circumstances. And James Mill, his instructor on general subjects, had on this point as little true knowledge as he had

himself. James Mill, above all men, believed that you could work out the concrete world of human polity and wealth from a few first truths; he would have shuddered at our modern conception of political economy, as a convenient series of deductions from assumed axioms which are never quite true, which in many times and countries would be utterly untrue, but which are sufficiently near to the principal conditions of the modern world to make it useful to consider them by themselves. At that time economists indulged in happy visions; they thought the attainment of truth far easier than we have since found it to be. They were engaged in a most valuable preliminary work, — one which is essential to the conception of the phenomena of wealth in such an age as this, or in any age in which free industry has made much progress: but after this preliminary work is finished, there is a long and tedious time to be spent in comparing the assumptions we have made in it with the facts which we see, and in adding the corrections which that comparison suggests; and only at the end of this dull task can we leave mere reasoning and come to life and practice.

Little is known of Ricardo's life, and of that little only one thing is worth mentioning in a sketch like this, — that he went into Parliament. He had retired with a large fortune from business comparatively young, — not much over forty, as far as I can make out, — and the currency and other favorite economical subjects of his were so much under discussion in Parliament that he was induced to enter it. At present an abstract philosopher, however wealthy, does not often enter Parliament: there is a most toilsome, and to him probably disagreeable, labor to be first undergone, — the canvassing a popular constituency; but fifty years ago this was not essential. Ricardo entered Parliament for Portarlington, which is now the smallest borough in Ireland, or indeed in the whole United Kingdom, and which was then a

mere rotten or proprietary borough; and no doubt Ricardo bought his seat of the proprietor. He was well received in the House, and spoke with clearness and effect on his own subjects. He is said to have had in conversation a very happy power of lucid explanation, and he was able to use the same power in a continuous speech to an assembly. His wealth no doubt gave him a facility in acquiring respect: Parliament, like every other collection of Englishmen, is much more ready to trust a rich man about money than a poor one.

The most curious characteristic of Ricardo's political career was his zeal to abolish the means by which he entered Parliament: he was most anxious for a parliamentary reform much resembling in principle that of 1832; and in this he agreed with most of the sensible men of his time. The narrow-mindedness and the want of capacity with which the Tory party had governed the country since the peace are now only known to us from history, and are not easily believed by those who have not carefully studied that history. As was the tree, so were its fruits: the government seemed to be one which must hurt a country; and in fact the country was, if not very unhappy, at any rate most uncomfortable. The best cure seemed to be a change of rulers, by a large addition to the popular element in the government; and as we now know, this has been effectual. The country has been far happier under the new system than under the old, and the improvement has been greatly due to the change: we could not have had Free Trade before 1832, and it is Free Trade which, more than any other single cause, makes us so happy. The change in popular comfort has been greater than Ricardo or than any one of his generation could have imagined; but we have had to pay a good price for it, and one of the items in that price is the exclusion of philosophers from Parliament. Such a thinker as Ricardo, with the unflinching

independence which characterized Ricardo, would be impossible in our recent Parliaments; no popular constituency would consent to elect such a man, nor would he consent to ask them.

Very little is now to be learnt of Ricardo's ordinary life: we know that he had a mind

> "Keen, intense, and frugal,
> Apt for all affairs,"

and we know little else. A well-authenticated tradition says that he was most apt and ready in the minutest numerical calculations. This might be gathered from his works; and indeed, any one must be thus apt and ready who thrives on the Stock Exchange. A less authorized story says that he was a careful saver of small sums, — "one of those people who would borrow a pamphlet, price sixpence, instead of buying it," notwithstanding that he was a rich man. We also know, as has been said, that he was very happy in orally explaining his doctrines, and they are by no means easy to explain in that way. He must have been most industrious, for he died at fifty-two; and either the thinking which he did or the fortune which he made would be generally esteemed, even by laborious men, a sufficient result for so short a life.

THE LATE MR. MILL.*

The sudden death of Mr. Mill has caused a deep feeling in all the intellectual part of England. Few living philosophers have had so much influence; fewer still have inspired so much personal respect — we might say so much personal affection — among many who had never seen and who were never likely to see him. The personal attachment of the inner circle of his followers was far greater.† To that inner circle we can make no claim to belong; we can only trace slightly, and in a manner which may not satisfy them, a rough outline of what seem to us the peculiarities of his mind and the sources of his influence.

To treatises such as Mr. Mill's "Logic" and his "Political Economy," it is not usually easy to give important praise which no one will deny: the subjects with which they deal, the "Logic" particularly, are too full of doubts and too fertile in animosities. But no one, we think, will deny that hardly ever, perhaps never, in the history of philosophy, have two books so finished and so ample been written by a man who had only his leisure moments to give to them, and who had a day's work to do besides.

* As Bagehot did not write the sketch of Mill he intended, the *Economist* obituary of May 17, 1873, is inserted here to round out his plan as much as possible. It is certainly no more meager and unsatisfactory than the sketch of Ricardo. — Ed.

† "I know no person whose friendship I valued more than that of Mill. I greatly respected his candor; I admired his translucent utterances. No man ever gave a clearer conception of what he meant at the moment. He was so earnest and so convinced, so gentle and so modest, that for a time one felt sure that he must be right. *But* —" etc. — Thorold Rogers, "History of Prices," Vol. v., Chap. xxviii.

The quantity of writing in these four thick volumes is not small: but many men, in detached essays and on varied points, equal or surpass that quantity, — even a daily occupation in laborious business is easily compatible with much desultory labor. But Mr. Mill's "Logic" and his "Political Economy" are not collections of desultory remarks; they are orderly, systematic works, in which the beginning has reference to the end, and almost every part has some relation, often a very close relation, to most other parts. To compose such books requires an incessant reminiscence of the past and an equally incessant foresight of the future; and both these, more almost than anything else, strain and fatigue the brain. Only men with their whole time and whole strength can usually accomplish such tasks; but Mr. Mill wrote both these books when a laborious man of business, who had daily difficult and exhausting duties to perform as well. Instead of wondering at occasional faults in such books, we should rather wonder that they exist at all.

The great merit of Mr. Mill, we think, was the merit of intellectual combination. Many philosophers — several contemporaries even — were much more eminent for absolute originality; but no one comes near Mr. Mill in the art — the invaluable art when, as now, philosophy is at once rich and fragmentary — of piecing together. In Mr. Mill's great works, theories are placed in just juxtaposition which were wide apart before, and thirteen are named in the same sentence where one would have hardly comprehended how they could be coupled together. Mr. Grote thus described the "Logic" in the *Westminster Review* — the other day, as we may say — in 1866: —

"The 'System of Logic' appears to us to present the most important advance in speculative theory which the present century has witnessed. Either half of it, the Ratiocinative or the Inductive, would have surpassed any previous work on the same subject. The Inductive half discriminates and brings into clear view, for the

first time, those virtues of method which have insensibly grown into habits among consummate scientific inquirers of the post-Baconian age, as well as the fallacies by which some of these authors have been misled. The Ratiocinative half, dealing with matters which had already been well handled by Dutrieu and other scholastic logicians, invests their dead though precise formalism with a real life and application to the actual process of finding and proving truth. But besides thus working each half up to perfection, Mr. Mill has performed the still more difficult task of overcoming the repugnance — apparently an inveterate repugnance — between them, so as chemically to combine the two into one homogeneous compound; thus presenting the problem of Reasoned Truth, Inference, Proof, and Disproof, as one connected whole. For ourselves, we still recollect the mist which was cleared from our minds when we first read the 'System of Logic,' very soon after it was published. We were familiar with the Syllogistic Logic in Burgersdicius and Dutrieu; we were also familiar with examples of the best procedure in modern inductive science; but the two streams flowed altogether apart in our minds, like two parallel lines never joining nor approaching. The irreconcilability of the two was at once removed, when we had read and mastered the second and third chapters of the Second Book of the 'System of Logic'; in which Mr. Mill explains the functions and value of the syllogism, and the real import of its major premiss."*

We do not altogether agree with Mr. Grote in his estimate of this particular doctrine, and on this particular instance we should have much to say if this were the place to say it. But the general description of the "Logic" which Mr. Grote gives is true and admirable: for the first time, an attempt was made to consider together the modern methods of scientific inference, and (as Sir John Herschel describes) the ancient methods of scholastic inference as mediæval writers set them forth. The two were never set so completely side by side before, or so fully made to illustrate one another.

Such a book, it will at once be seen, requires a most delicate art of exposition; for these comparisons, the style of a writer must describe not only

*January, 1866.

"meanings" but shades of meaning, — not large ideas in the rough, but nice ideas with nice finish: and for this Mr. Mill was well fitted both by genius and by culture. He inherited a philosophical acumen from his father (and, we suspect, from a long line of Scotch and argumentative ancestors), and an education in France had given him the French gift of precise and graceful explanation. That he also caught a little, though only a little, of the tendency to diffuseness of modern French philosophers must, we admit, be acknowledged; but he also gained the literary talents most useful to a comprehensive philosopher, — their extreme clearness and their wonderful readability.

In political economy there was an eminent field for Mr. Mill's peculiar powers of comparison. There is little which is absolutely original in his great work; and much of that little is not, we think, of the highest value. The subject had been discussed in detail by several minds of great acuteness and originality: but no writer before Mr. Mill had ever surveyed it as a whole with anything like equal ability; no one had shown with the same fullness the relation which the different parts of the science bore to each other; still less had any one so well explained the relation of this science to other sciences, and to knowledge in general. Since Mr. Mill wrote, there is no excuse for a political economist if his teaching is narrow-minded or pedantic; though perhaps, from the isolated state of the science, there may have been some before.

Mr. Mill had another power which was almost of as much use to him for his special occupations as his power of writing: he was a most acute and discerning reader. The world hardly gave him credit for this gift before the publication of his book on Sir William Hamilton; but those who have read that book will understand what Mr. Grote means when, in the essay we quoted before, he speaks of

Mr. Mill's "unrivaled microscope which detects the minutest breach or incoherence in the tissue of reasoning." And he used this great faculty both goodnaturedly and conscientiously: he never gave heedless pain to any writer, and never distorted any one's meaning.

In fact, and partly for the reasons we have stated, Mr. Mill's two great treatises have had a unique and immense influence. In political economy the writer of these lines has long been in the habit of calling himself the last man of the ante-Mill period. He was just old enough to have acquired a certain knowledge of Ricardo and the other principal writers on political economy before Mr. Mill's work was published; and the effect of it has certainly been most remarkable. All students since begin with Mill, and go back to all previous writers fresh from the study of him: they see the whole subject with Mr. Mill's eyes; they see in Ricardo and Adam Smith what he told them to see, and it is not easy to induce them to see anything else. Whether it has been altogether good for political economy that a single writer should have so monarchical an influence, may be argued; but no testimony can be greater to the ability of that writer and his pre-eminence over his contemporaries. In a wider field the effect of the "Logic" has been enormous,—half the minds of the younger generation of Englishmen have been greatly colored by it, and would have been sensibly different if they had not been influenced by it; and there is no other book of English philosophy of which the same can be said, even with a pretext of truth.

A complete estimate of Mr. Mill would include an account of his career in Parliament, and also an account of some peculiarities of his mind which gave him, considering the dry nature of most of his pursuits and studies, a most singular influence. To very many younger minds he was not so much a political economist as a prophet, not so much a

logician as a seer. He had, besides his rare power of arguing and analyzing, an equally rare kind of contagious enthusiasm, which influenced a multitude of minds and made them believe as he did. But an estimate of these peculiarities would be little suited to these pages; nor should we at this moment like to say much which, in our judgment, it would be necessary to say in order to make this estimate just. We have preferred to say that which is plainly true, and which could give no pain to any one.

THE GROWTH OF CAPITAL.

The conclusions that English political economy is an analysis only of industrial societies which are to a certain extent developed, will be strengthened by a consideration of the doctrines which that political economy teaches us as to one of the principal parts of the subject,—the theory of the growth of capital. Our political economy does not recognize that there is a vital distinction between the main mode in which capital grows in such countries as England now, and the mode in which it grew in all countries at first.

The principal way in which capital increases in England now is, by abstinence from enjoyment. We receive our incomes in money, and either we spend them on our enjoyments,—in which case capital is not increased, for our incomes are all gone and no new productive thing is made; or we abstain from enjoyment and put our money into trade ourselves, supposing that we are in trade, and supposing that we are not in trade, lend it to those who are. The productive part of wealth—the wealth which creates other wealth—is augmented mainly by our not enjoying our incomes.

But there is another mode of augmenting capital, of which Defoe gives us perhaps a more vivid notion than we can get elsewhere.

"I cannot say," says Robinson Crusoe, "that after this, for five years, any extraordinary thing happened to me; but I lived on in the same course, in the same posture and place, just as before. The chief things I was employed in, besides my yearly labor of planting my barley and rice, and curing my raisins, of both which I always kept up just enough to have sufficient stock of one year's

provision beforehand, — I say, besides this yearly labor, and my daily pursuit of going out with my gun, I had one labor, to make me a canoe, which at last I finished; so that by digging a canal to it of six feet wide and four feet deep, I brought it into the creek, almost half a mile. As for the first, which was so vastly big, as I made it without considering beforehand, as I ought to do, how I should be able to launch it; so never being able to bring it into the water, or bring the water to it, I was obliged to let it lie where it was, as a *memorandum* to teach me to be wiser the next time. Indeed, the next time, though I could not get a tree proper for it, and was in a place where I could not get the water to it at any less distance than, as I have said, near half a mile, yet as I saw it was practicable at last, I never gave it over; and though I was near two years about it, yet I never grudged my labor, in hopes of having a boat to go off to sea at last." *

But in this case there was evidently no abstinence from enjoyment. Robinson Crusoe had only the bare means of subsistence, — he had no pleasant things to give up; but he employed his time and labor in making a vessel, — a piece of capital if ever there was one.

Just similar is the practice of primitive societies. When a savage in the Stone Age made a flint implement, he relinquished no satisfaction; having nothing else to do, he made a tool, which has been the beginning of all other tools.

"Mankind," says a recent writer,† "may have discovered how to manufacture earthen vessels in various ways. Sir John Lubbock points out that Captain Cook saw stones surrounded with a rim of clay in use among the Aleutians on Unalashka; but this might be an imitation of European vessels with which the islanders had already become acquainted through Russian sailors. The practice of the Australians on the Lower Murray River, of puddling holes in the earth with clay and cooking food in them, might perhaps have led an inventive mind to the manufacture of earthen vessels. But the process is better explained by the account of the French sailor Gonneville, who in 1504 landed on a South Atlantic coast, probably in Brazil.‡ He describes certain wooden vessels in use

* Section xv.

† Oscar Peschel's "Races of Man and their Geographical Distribution," page 168.

‡ Pierre Margry, "Les Navigations Françaises," 1867.

among the natives (in whom D'Avezac fancies that he recognizes Brazilian Carijo) enveloped in a coating of clay as a protection from the fire; * if by chance the wooden bowl separated itself from the covering of clay, an earthen vessel would remain. In examining the site of an old pottery manufactory of the red Indians on the Cahokia, which falls into the Mississippi below St. Louis, Carl Rau discovered half-finished vessels,—that is to say, baskets of rushes or willow, lined inside with clay."

These primitive potters had no luxuries to forego, and had no "income" to spend on luxuries; they simply had spare time and unused handiness, and with this they made the first pots, which were the beginning of all pots,—the ancestors first of the tea-kettle and then of the condensing engine.

In the same way there was no sacrifice of pleasure in the greatest source of early capital, the taming of animals; on the contrary, according to the most probable theory, there was a new pleasure in taming them which did not require the surrender of any old pleasure. Mr. Galton has shown that in all probability the taming of animals began not in the restraining of any impulses, but in the indulgence of some very simple ones.

"The domestication of animals," he tells us, "is one of the few relics of the past whence we may reasonably speculate on man's social condition in very ancient times. We know that the domestication of every important member of our existing stock originated in prehistoric ages, and therefore that our remote ancestors accomplished in a variety of cases what we have been unable to effect in any single instance.

"The object of my paper is, to discuss the character of ancient civilization, as indicated by so great an achievement. Was there a golden age of advanced enlightenment? Have extraordinary geniuses arisen who severally taught their contemporaries to tame and domesticate the dog, the ox, the sheep, the hog, the fowl, the camel, the llama, the reindeer, and the rest? Or again, is it possible that the ordinary habits of rude races, combined with the qualities of the animals in question, have sufficed to originate every instance of established domestication?

* D'Avezac, "Voyage du Capitaine Gonneville," 1869.

"The conclusion to which I have arrived is entirely in favor of the last hypothesis. My arguments are contained in the following paper; but I will commence by stating their drift, lest the details I introduce should seem trifling or inconsequent. It will be this: — All savages maintain *pet* animals, many tribes have *sacred* ones, and kings of ancient states have *imported* captive animals, on a vast scale, from their barbarian neighbors. I infer that every animal of any pretensions has been tamed over and over again, and has had numerous opportunities of becoming domesticated; but the cases are rare in which these opportunities can lead to any result. No animal is fitted for domestication unless it fulfills certain *stringent conditions*, which I will endeavor to state and to discuss. My conclusion is, that all domesticable animals of any note have long ago fallen under the yoke of man; in short, that the animal creation has been pretty thoroughly though half-unconsciously explored by the every-day habits of rude races and simple civilizations."

And after enumerating the qualities which a tamable animal must possess, — which are hardiness, fondness for man (which some animals now used have, while others have not), desire of comfort, easiness to tend, willingness to breed, and usefulness to the human race, — he adds: —

"The utility of the animals as a store of future food is undoubtedly the most durable reason for maintaining them; but I think it was probably not so early a motive as the chief's *pleasure in possessing* them. That was the feeling under which the menageries described above were established. Whatever the despot of savage tribes is pleased with becomes invested with a sort of sacredness; his tame animals would be the care of all his people, who would become skillful herdsmen under the pressure of fear, — it would be as much as their lives were worth if one of the creatures were injured through their neglect. I believe that the keeping of a herd of beasts, with the sole motive of using them as a reserve for food or as a means of barter, is a late idea in the history of civilization. It has now become established among the pastoral races of South Africa, owing to the traffickings of the cattle traders; but it was by no means prevalent in Damara Land when I traveled there twelve years ago. I then was surprised to observe the considerations that induced the chiefs to take pleasure in their vast herds of cattle: they were valued for their stateliness and color far more than for their beef; they were as the deer

* "Domestication of Animals," Tr. Lond. Eth. Soc., Vol. iii., N. S., 1865.

of an English squire, or as the stud of a man who has many more horses than he can ride. An ox was almost a sacred beast in Damara Land, not to be killed except on momentous occasions, and then as a sort of sacrificial feast, in which all bystanders shared. The payment of two oxen was hush-money for the life of a man. I was considerably embarrassed by finding that I had the greatest trouble in buying oxen for my own use, with the ordinary articles of barter: the possessors would hardly part with them for any remuneration; they would never sell their handsomest beasts." And he concludes: — "I see no reason to suppose that the first domestication of any animal, except the elephant, implies a high civilization among the people who established it. I cannot believe it to have been the result of a preconceived intention, followed by elaborate trials, to administer to the comfort of man. Neither can I think it arose from one successful effort made by an individual, who might thereby justly claim the title of benefactor to his race; but on the contrary, that a vast number of half-unconscious attempts have been made throughout the course of ages, and that ultimately, by slow degrees, after many relapses, and continued selection, our several domestic breeds became firmly established." *

This theory is one of the most valuable fruits of that contact of the most cultivated living minds with the least so — of men of science with savages — which is characteristic of this generation; and though its details may be modified, its essence seems certain, and it shows that this great form of early capital — the *live* form — did not begin with abstinence at all.

Even in such times as are described in the Book of Genesis, — the specially pastoral times, — abstinence was not the main source of capital. When we are told that the flocks and herds of certain patriarchs "grew and multiplied" exceedingly, those patriarchs were sacrificing nothing. They had enough to eat and to drink, the women of their household made their clothes; they had few other conscious wants, and still fewer means of supplying those which they had. The vast increase of animal power which helped on after-wealth so much had probably its origin in

* "Inquiries into Human Faculty," section "Domestication of Animals," slightly rewritten from Tr. Eth. Soc. before quoted.

the pride of the eye, in the love of the spectacle of wealth, as much as in anything. Abraham and Jacob were pleased to see "their cattle wax great and cover the whole land," and therefore they let them cover it; there was no luxury to them equal to this,—there was not even a competing one.

Another analogous source of capital in early times was making slaves and breeding slaves; yet neither in the capture nor in the breeding was there any kind of relinquishment of enjoyment. The slaves were gained in the fortune of war; and if A had not enslaved B, B would have enslaved A. The joy of the combat was perhaps the greatest known in those times; and even in the cruelest times, it was probably pleasanter to spare the life of the captive than to take it.

A similar source is marriage; which indeed is all but the same, for even the highest wives of primitive ages worked in the house much like slaves, and the concubines — who really were slaves — were but faintly divided from these wives. But it would be absurd to call keeping a harem a kind of abstinence, though harems were a great form of capital, and the members of them made a great deal of wealth.

The reason why we now so closely connect "abstinence" with capital is, that the final product of our industry is almost always received in what I may call an "optional" medium. Almost all our wealth is created to be exchanged, and that exchange is effected by means of money; we can either use that money to buy perishable things which produce nothing, or we can "invest" it, as we say, in some producing business, or lend it to some one — generally to some one engaged in production — who will pay an interest upon it. But in a state of society where things are *not* created to be exchanged, "abstinence" plays no such constant part. Men must, it is true, abstain from eating the food which is necessary for their subsistence hereafter, and the food so obtained

is certainly "capital" obtained by abstinence; but most permanent things which are made are like the "flint implement" and the primitive clay vessel,—things which contribute to daily comfort because they are in daily use. The industry which created them never assumed an optional form; it was from the beginning fixed in the particular form in which it was created: neither can be sold or exchanged, for we are supposing a state of society in which there is no exchange or sale.

A primitive patriarchal society is in fact very like this. Either exchange or sale was a very rare act in the lives of such persons as Lot or Abraham: they rarely saw any one to exchange with. They rarely went down into Egypt to buy anything; they rarely saw any sort of traveling merchant to whom they could sell anything. The life of such persons is a life of production not for sale but for use, as far as it is a life of production at all.

Hire is a still rarer phenomenon at such a period. Hire as a rule involves proximity of residence, so that the lender may be sure the hirer will return his article; if the borrower goes off to an unknown distance, no one can be sure that he will do so. Nor for the most part is *trust*, which is essential in a loan, developed in societies till men have long lived near together, till they have learnt to know one another, and till they have created some sort of law or formed some effectual custom which partly punishes and partly prevents bad faith. The diffused habit of lending things, which is the basis of so much of modern industry, is in truth a habit hard to diffuse, and one which the earliest men could not learn.

Nor even when the hire of capital does begin to be an important part of industrial organization, is there necessarily any abstinence from enjoyment in the possessor. Sir Henry Maine describes, in his "Early History of Institutions," a condition of Irish

society which was based on the loan of "cattle,"—the main capital then existing,—in which there was no abstinence in the lender at all.

"Every considerable tribe," he tells us, "and almost every smaller body of men contained in it, is under a Chief, whether he be one of the many tribal rulers whom the Irish records call Kings, or whether he be one of those heads of joint families whom the Anglo-Irish lawyers at a later date called the Capita Cognationum. But he is not owner of the tribal land. His own land he may have, consisting of private estate or of official domain, or of both; and over the general tribal land he has a general administrative authority, which is ever growing greater over that portion of it which is unappropriated waste. He is meanwhile the military leader of his tribesmen, and, probably in that capacity, he has acquired great wealth in cattle. It has somehow become of great importance to him to place out portions of his herds among the tribesmen, and they on their part occasionally find themselves, through stress of circumstance, in pressing need of cattle for employment in tillage. Thus the Chiefs appear in the Brehon law as perpetually 'giving stock,' and the tribesmen as receiving it. The remarkable thing is, that out of this practice grew not only the familiar incidents of ownership, such as the right to rent and the liability to pay it, together with some other incidents less pleasantly familiar to the student of Irish history, but, above and besides these, nearly all the well-known incidents of feudal tenure: it is by taking stock that the free Irish tribesman becomes the Ceile or Kyle—the vassal or man—of his Chief, owing him not only rent but service and homage." *

Upon the very surface of this description, it is palpable that the chieftain gave up no enjoyment when he hired out these cattle; he doubtless kept quite enough fully to feed himself with all his people, and after that he wanted no more. The power and place he gained by this *quasi* feudal use of them were the keenest kinds of pleasure then possible to him.

"Cattle" fill so subordinate a place in English industry that many English writers evidently never think of them when they speak of "capital"; they

* Lecture vi.

have in their minds the machines which they see, and they forget that once men bred capital more than they made it: yet not only are "cattle" and "capital," of course, etymologically the same word, but cattle fill a very curious place in the history of the subject.

First. They are a kind of capital at once co-operative and remunerative: they can be used either to aid labor or to reward it; they are both helps to industry and means of pleasure. Their vital force is the best of early machines, and their milk and their flesh are the greatest of primitive luxuries. There is scarcely anything which primitive laborers more desire, and scarcely anything which helps them so much. And it is very curious that the sort of capital which first bore the name, and etymologically is the beginning of all the rest, should be a link between, and combine, the nature of two things now so dissimilar that at first it hardly seems right that they should have the same name, — the bread which the laborer eats and for which he works, and the spindle or the loom with which he works.

Secondly. Cattle unquestionably, on account of this double desirability, are among the earliest forms of money; probably the very earliest in which "large transactions," as we should now speak, were settled. It was the first or among the first of "wholesale" moneys.

In this way, though English political economy often neglects the use of cattle as capital, and though some of its doctrines are inapplicable to "cattle" in the primitive condition of industry, cattle have nevertheless been a main agent in creating the developed state of industry in which English political economy was thought out, and to which alone it is entirely applicable. Cattle rendered possible primitive agriculture, which first kept men close together, and so made the division of labor possible; were the beginning of "wages-paying capital," which

that "division" first requires and then extends; were among the first things hired, and the first money. We should be careful to watch in this single article the transitions of industry; for the so doing may save us from the greatest of all mistakes, — that of riveting as a universal form upon all societies, axioms only fitting societies like our own.

These illustrations might be multiplied almost endlessly; but what have been given are enough to prove that capital is created by any series of acts by which men make or bring into existence useful things, and that only some of these acts are accompanied by abstinence, while others are not.

Thirdly. Neither is the loan of capital always accompanied by abstinence: it may or may not be according to circumstances.

* * * * * * *

If, to simplify the matter, we look at the state of things which is going on around us, we see that capital augments in this way. People's incomes are paid in money: out of that money some is spent on necessary subsistence, some on temporary enjoyment, and some on durable means of comfort; the rest is left in "money," and this we call the saving, the new "capital." The amount of it depends on three elements: first and evidently, on the amount of the income out of which the saving is to be made; secondly, on the degree in which future wants preponderate over present ones; and lastly, on the *efficiency* of saving, the *success* it obtains.

The first and greatest future want is what I may call the "old-stocking" one; that is, the craving to have some stock of money laid against the unknown future. The strength of this craving differs much in various races of men; and as a rule, the strong races used to prosperity have much less of it than the weak ones familiar with adversity. You will find much more laid up in the cabin of an Irish peasant

than in the cottage of an English artisan, though the latter has five times the greater means: and this is natural, because the English artisan believes, and probably believes with truth, that he is sure to be able to earn money; whereas the Irishman's notions are based on a world where it has often been impossible to earn a farthing, and in which those ready to live even on potatoes could not get potatoes to live on. Even in higher life, very considerable sums for their circumstances are often saved by timid, weak people. I know a case in which a sum of (I think) £120 was made up for a gentleman who had become incapacitated; he enjoyed it a few years, and when he died, from £700 to £800 was found in his room: he always feared that his income or a part of it might cease, and wanted to be able to live if it did. Against all contingent evils this "stocking" fund is a resource; and against old age, the most likely of those evils. The next greatest — or probably an equally great — future want is the desire to provide for the next generation: people insure their lives who save in no other way; there is probably no greater anxiety in the world than the wish of parents to start children in the same level of life in which they started themselves, and few greater ambitions than to start them on a higher level. Lastly, there is the desire to be rich, especially in countries where wealth makes the man, where it not only buys commodities but where without it some of the best unbought things — respect and deference — are not easy to be had. I need not enumerate the present wants which come into collision with these, nor go into any detail as to them.

But we must observe what is incessantly forgotten, that it is not a Spartan and ascetic state of society which most generates saving. On the contrary, if a whole society has few wants there is little motive for saving; the reserve, the old-stocking store of those who want little, need only be small. Those who

want to start their children with little need save little: those who reckon £100 a year "riches" need not and will not deprive themselves of anything to obtain more; a state of society which encourages that feeling is not likely to be rich. Nothing is commoner than to read homilies on luxury, because it is a "waste of money," and "bad for the poor"; but without the multifarious accumulation of wants which are called "luxury," there would in such a state of society be far less saving than there is. If you look at the West End of London, with its myriad comforts and splendors, it looks at first sight like a mere apparatus for present enjoyment; and so far as the present feelings of those who live there go, it often is, — very many of the inhabitants are thinking only of themselves: but there is no greater benefit to the community, for all that, than this seemingly thoughtless enjoyment. It is the bait by which the fish is caught; it is the attraction by which capital is caught. To lead a bright life like that, at least that their children may lead it or something like it, many times as many as those who now live it, spare and save; and if it be good for the poor that capital should be saved, then the momentary luxury which causes that saving is good for the poor. The analogy of animal life is reversed, for it is the butterfly which begins as the grub.

On the other side we must remember — what in books of political economy is sometimes forgotten — that saving is not necessarily good: the capital may come too dear. A clergyman who gives his children a good education does more really to increase wealth, not to say anything of anything else, than if he saved the money. The engineer, the lawyer, the physician, are in their various ways productive people; and the nation would have been poorer, not richer, if their father had kept the money which educated them, in order to leave them at his death so much more. The same may not be so conspicuously true

of the daughters, but it is as much so really: a good mother of a family causes more wealth than half the men, for she trains from the beginning boys to be fit for the world, and to make wealth; and if she fails at that beginning, the boys will be worse gold-finders all their lives.

It must be observed, too, that there is an intellectual element in the matter: besides the two kinds of wants, future and present, there is the faculty of making the comparison; and the habits of some people's lives fit them much more for this than those of others. An actor, who is concerned with the momentary impression on passing audiences, has nothing to bring the future close to him at all. An artisan has little more: his daily work passes with the day. But a capitalist in business has the future forever brought home to him: he has to look into the future, perhaps a distant one, for the profit on the goods which he buys, and to find in the near future the money with which these goods are to be paid for; the first thing in his mind is a list of "acceptances" soon to be provided for, the next is the balance-sheet to be made up some time hence. A banker above all men incessantly lives in the future: he is, or ought to be, forever thinking how he should pay his deposits if he were asked for them; he must think daily how he will find means for the current demands of every day; he too has a balance sheet to be looked to, upon the results of which he will have to live. A man thus living in the future has a greater disposition to provide for it; and this is the one main reason why the man of business, of whatever species, — the manufacturer, the merchant, or the banker, — will save much more than any kind of person who lives upon the fruits of a momentary skill or talent.

In many minds this feeling coalesces with the "old-stocking" want; that is to say, the desire to provide for definite engagements (those engagements

being an incessant series) passes into and is blended with the desire to provide for the unknown. The pecuniary classes have a general feeling of "liability" about their minds to which other classes are strangers; and justly, because their risks — not only their known but their unknown ones — are greater. I once heard a very experienced man lay down this principle: — "A man of business," he said, "ought not to be over-cautious; he ought to take what seem good things in his trade pretty much as they come: he won't get any good by trying to see through a millstone. But he ought to put all his caution into his 'reserve fund': he may depend on it he will be 'done' somehow before long, and probably when he least thinks it; he ought to heap up a great fund in a shape in which he can use it, against the day at which he wants it." It is the disposition so generated which is in a trading nation among the strongest motives to save.

Besides these two factors in the growth of capital, — the amount of the income out of which saving has to be made, and the disposition to sacrifice what is present to what is future, — there is, I have said, a third; viz., the efficiency of saving in creating capital. There is a whole scale of various degrees of this efficiency in actual life. At the bottom is the brisk peasant who puts away his money into an old stocking, who has no means of employing it, who will not trust any one else with it: here, all that the saving of £10 will produce is £10; it is sure never to get any more. At the top of the scale is the able capitalist in a large and growing business: every penny he can put into it yields him a high profit, because he gets an income from unusual ability [and] unusual opportunity, as well as the common rate; such a man will almost always save more than others, because he has a far greater reward *per cent.* for saving it. The rate of profit depends on the efficiency of industry: when more is made at less cost, the

profit is greater; when less at greater, the profit is less. I am not sure whether, to many minds, this language will not present a difficulty; I know it long did so to my own, — I was conscious of a haze about it. "It is stated," I said to myself, "that there is 'more' of something or other, but of *what* is there more?" and I could not answer the question very well. More "exchangeable value," more "money's worth," were the natural answers; but I was not satisfied that they were the complete ones. We must analyze a little further. The easiest case to analyze is the gold-mining, the money-making business. If 10,000 sovereigns are invested in gold-mining, — in paying wages, in buying machinery, and in accompanying expenses, — and if that produce per annum, gold which can be made into £11,000, this measures the rate of profit in the country. If the efficiency of industry were less, so many additional sovereigns would not be produced; if more, a proportionately greater number would be produced. In the profit of all trades there is the same fundamental fact, an addition to the "exchangeable value" of the commodities of a country; but in the profit of the gold-mining business we can see that fact most easily, because we can take the capital before it is invested, as so much gold, and it comes back as that much *plus* some more. In other cases there is a change necessary into money; in this case the profit palpably results from the mere production.

We must observe, however, that this profit in the gold-mining trade is only a measure of the general rate of profit in the country, and of the general efficiency of industry which causes that rate; it has no peculiarity about it except that which has been said. If the profit in this trade were more than in any other, capital would go thither, the production of gold would augment, and prices, measured in gold, would rise; this would raise the price of gold-mining machinery, the rate of gold-miners' wages, and all

the incidental outgoings of the trade: and as the number of sovereigns which that "machinery" and those "miners" could produce is not increased, the profit in the trade will fall. And the reverse will happen if that profit be less: a contrary series of changes will make it rise.

In a country in which the productive arts are high, other things being equal, profits will be high also: if the outlay of the capitalist on all means of production is the same, his remuneration will be greatest where more is produced. Suppose by a sudden series of inventions the productive power of industry were augmented in all trades 10 per cent. (including the gold-mining trade, so that we may be clear of all questions as to money and price), the revenue of the capitalist would be augmented by that 10 per cent., on condition of course of his outlay in all ways remaining the same, including that on wages; and his power of saving would be augmented equally.

Single sudden inventions which help in everything do not happen; but the general progress of the productive arts in the last thirty years has been very like it, as far as effects go. Almost everything has been made more easily; many things far more easily. Even the growth of raw produce for sale has been facilitated, if not as much as some other things, yet still very much: railways have made land which was far from the market able to compete with that near it. The daily subsistence of such a city as London would have been excessively costly in the pre-railway time; perhaps it would have been impossible. The amount of things produced on purpose to be exchanged, now, as compared with fifty years ago, is so much increased that our fathers would not have comprehended it or believed it. The rise of prices would have been enormous, if the same extension of productive power had not extended to the money trades, to gold and silver. For many years before

1840 the production of these metals had been excessively slow, and their value was rising: Mr. Jevons thinks "that prices had on the average fallen between the years 1820 and 1844 in the ratio of 103 to 69, or by 33 per cent.; whereas between 1844 and 1857 they rose in the ratio of 69 to 85, or by about 23 per cent."* Thus, the effect of the great gold discoveries consisted more in arresting the previous continuous *appreciation* of the precious metals than in causing a positive depreciation; indeed, in 1863, Mr. Jevons stated the depreciation of gold at the very moderate amount of 13 to 16 per cent.†

If the increase in the productive power of general industry had come upon an age straitened as to money-making industry, the fall of prices would have been such as we have no example of, and the effects would have been harassing and confusing; but fortunately, the production of gold and silver has been even more facilitated than that of most other things. There has been no such confusing fall of price as, except for the new discoveries of gold in California and Australia, there would have been. The effect of the productiveness of industry has been greatly to retard and almost to prevent the equally confusing rise of price which would otherwise have happened; the productive power of men of business has thus been incalculably augmented, and with that their saving power.

The second main source of capital in the present day is the saving of men — of persons — out of business. Such persons, not being able to make anything themselves, must put such part of their income as they wish to save into the hands of others, and far the most important way in which they do this is by lending; they lend it on interest, and what they can save varies, other things being the same, with that

* "Journal of the London Statistical Society," Vol. xxviii., page 315.

† "Serious Fall in the Value of Gold," etc., page 30.

interest. What then will that amount be? This is determined as other market prices are determined.*

The most important factors in fixing it are the amounts of money to be lent, and the amounts which borrowers are willing to borrow upon such security as the lenders are willing to accept. The most important of these borrowers are men of business. These will be most anxious to borrow money when the rate of profit is high, and when therefore they can employ it to the most advantage; at such times they will strain every nerve to obtain as much as possible. But in the earlier states of industry they have great difficulty in obtaining it: they have no security which will satisfy those who wish to lend. In such epochs the only sort of "security"—the only way in which the borrower can make the lender sure of his money is, by depositing with him fixed property, or at least giving him the control over it; he must pledge movables, or transfer the *indicia* of ownership over immovables. But in such a commercial civilization as ours there is an immense and very powerful machinery for conducting the money of the accumulating class into the hands of the using class. Bankers and bill-brokers form a class whose business it is to know the credit of different persons, and to say when and how far they singly or together can be trusted. Millions are lent in this country upon bills of exchange with only two signatures,—that is, upon an order to pay money accepted by the person to whom it is addressed, and which the person who gives the order engages to pay if the other does not; the money is therefore in fact advanced on an estimated probability that one or other of these two persons will pay, of which the skilled advancing class—the bankers and the bill-brokers—form their judgment. We are so familiar with it that we forget how marvelous it is; but probably our modern civilization, notwithstanding its railways, telegraphs,

* See Appendix.

and other like things, has nothing similar. That an endless succession of slips of written promises should be turned into money as readily as if they were precious stones would have seemed incredible in commerce till very recent times. Our ancestors would have understood that something like it might happen with the promises of a few millionaires or governments; but they would have never thought it possible that such an infinity of names could be known or promises estimated. And the wonder is greater because they are not estimated equally: the relative possibility of different "parties" not paying is materially determined to the minutest gradations, and a bill is done at $3\frac{1}{2}$ or 4 per cent. accordingly. The intermediate dealers — the bill-brokers and bankers — live upon this knowledge: they gain if they are right and are ruined if they are often much wrong, and therefore they *are* right. Through these expedients an immense tide of money flows into commerce at most times, though occasionally they are impaired and it is impeded.

Our commercial civilization also tends more and more to improve the means by which actual property can be pledged; the *indicia* of ownership are made more easily transferable. The English law of real property does not bear a very good reputation, but it is indisputable that in this respect it is more advanced than any similar law in the world. In the last century the courts of equity decided that the deposit of title-deeds, with or even without a written memorandum, was an adequate security for a loan; and on this sort of "equitable" mortgage a very large sum is lent for short periods, — especially by country bankers, who know the people to whom and the land on which they are lending. Most individual transactions of this sort are small, but the sum total is very great. Dock and warehouse warrants for goods deposited are also fruits and indications of a highly improved commercial state; they, and all

similar means of pledging property, tend to augment the borrowing power of men of business, and so to raise the rate of interest.

Besides men of business, who borrow in order to *make*, a large class of people borrow in order to *hold:* the pride and pleasure of possessing property are so great that people will very often pledge that property in order to obtain it. A large part of the titles of our richest land-owners are mortgaged in this way to "insurance offices," who have much money constantly to lend. The arrangement suits both parties, for no one knows of the loan; as the insurance office is permanent, the loan is rarely called in: and thus the land-owner gets the pomp of ownership, while the office enjoys the perfection of a security.

There are also a class of persons who borrow in order to spend; that is, to spend the principal (for all borrowers spend the interest, else they would not want to borrow). In such countries as England, where the producing and preserving classes are such large borrowers, the demand of spendthrifts has but little influence on the rate of interest,—it is overpowered by the comparative greatness of other demands; but in simpler states of society the demand of the "prodigal" fills a conspicuous place in the money market, and in some of the books which have come down to us from those early times he seems the principal borrower that is thought of. But the growth of civilization, though diminishing this species of spending borrowers, creates another much more efficient species: governments obtain a vast credit, and borrow for war and other non-productive purposes, such as the early history of mankind could never have imagined. The loss of France by individual "prodigals" will not for ages be as great as her loss by the folly of the seven-months' war with Germany. This is of course so much to be deducted from the capital of the country; but nevertheless the sum so borrowed tends to raise the rate of interest,

and thus to augment the means of future saving by those who wish to save.

At the present day, therefore, the amount of saving in a nation depends, as we have seen, on the amount of the annual income out of which saving is to be made. The disposition to save out of it (varying in different classes), and the efficiency of saving in creating new capital, depend partly on the rate of profit and partly on the rate of interest. And from this saving arises the annual increment of capital,—the amount of yearly addition to it; but there is also a yearly decrement,—an annual waste. The amount of this depends, in such a country as England, mainly on the amount of unsuccessfulness, of absolute loss, in business. Certain adventures not only bring no profit, but never return the capital spent on them. The liabilities of bankruptcy estates in England, including liquidations and compositions, but excluding public companies, in 1870 were £17,456,000: the apparent assets were £5,382,000; the difference, therefore, or £12,074,000, was so much pure loss. And there is much other loss in business which does not figure here. To this must be added the loss in such a country and age as ours,—usually loss*—by private prodigals and by state follies. If we could only know the amount of the diminutions and augmentations in any nation, [and] could deduct the one from the other, we should know the increase of the capital during this time by that nation.

We must be careful, however, to observe that our account of the growth of capital is only applicable to such times as ours; to times when the division of labor has been carried out, and where almost everything is produced by one man for sale to others. The result of this is, that every sale changes a man's product into a form in which he has the

* I feel sure these two senseless words are either a misreading, or that Bagehot accidentally failed to cancel them. Perhaps "usually" is a misreading of "unnoted."—Ed.

choice of saving or not saving it; the money which is the proceed of the sale may either be spent on immediate enjoyment, or set aside in some way for the future. The incomes of men are in an adult economical society received in an *optional* medium; but in early societies this is not so. Things not being produced for sale, are only what they are by nature; there is no choice in the way of using most of them: they are by their essential character either fit for present use or fit to be set apart for the future, they are very rarely in the same degree fit for both. Defoe illustrates this better than many graver authors.

Secondly, our account of the growth of capital assumes that men can always find something to save in; that a person who wants to provide for his future wants can do so if he will give up present ones: but this is not true in early times at all. Most primitive wants are for rapidly perishable things; and it is of no use to keep a store of those things. If you do you will be "keeping stale fish,"—you will have sacrificed the present without obtaining the future; you will have that which was of use once, but now is so no longer. Food is the greatest want of early times; but most food, vegetable or animal, will not of itself last long. It is of no use for a tribe of hunters to set aside the game they kill; it is not till the pastoral age has arrived that men have any means of storing up the food they require. The first "granaries" of men were, if the phrase be allowed, "live granaries": the flocks and herds which walked the fields, and could be left, when not wanted to be slaughtered, where they were. Clothes, the second great want of man, are always short-lived, and it is not much use to store them up. There was in early times no mode of supplying those wants for the future; men had to live from hand to mouth.

COST OF PRODUCTION.

I.

MANY persons are much puzzled by the phrase "exchange value": not only outsiders and learners, but even practical thinkers on the subject, use it awkwardly, and do not feel that the idea is vivid in their minds. And if we look at the matter historically, it is very natural that this should be so: no nation — no set of persons — who did not possess a fixed and efficient money ever attained the idea. Nations which only use barter know that a certain amount of one or two common things mostly exchanges for a certain amount of one or two other things; but they have no conception of the "value" of one thing as against *all* other things. This idea is only gained by the use of money as a general common measure: by measuring all things — not one — against one, men come to be able to measure them against one another. "Price" — price in money — is the foundation of the economical idea of exchangeable value; but though it is the foundation of that idea, it is not the whole of it. "Money" is a commodity like any other; and it tends to fluctuate in the ratios in which it exchanges with other commodities, from chances affecting itself, just as they do in relation to it. At any single moment, if you know the "prices" of all articles you know their relative exchangeable value: but when you come to compare one time with another, — say the prices of to-day with those of this time last year, — you might be much puzzled, for possibly all might have risen or all might have fallen; and this would have arisen

not from anything which related to the things measured, but from something affecting the measuring instruments. What we mean by "exchangeable value" in political economy is not actual price, but perfect price; the ratio in which everything exchanges against all other things,— measured not as it is, by the intrinsically valuable measure of money, but as it would be against a similar measure which was invariable intrinsically.

We must bear in mind that on no two days — indeed, at no two minutes — are the rates at which things exchange for one another at all the same: the price list of the Stock Exchange varies from hour to hour, and so do the prices in other markets. General "exchangeable value," which is the sum total of price lists, is therefore incessantly altering. The fact which it denotes is one of the greatest complexity with which any science can have to deal; and it is no wonder, therefore, that most imaginations find it hard to get and keep a hold of it. Incomparably the best way to aid them in this is, to make a hypothesis and to assume that money is of invariable value. Of course this is a hypothesis not coinciding with fact, — on the contrary, it leaves out a whole range of facts; but if we are careful with it,— if we remember what are the omitted facts, and make corrections for them if necessary, — the hypothesis is of the greatest use. The figures of price are in this case like the symbols of algebra: they hedge in the mind to a definite thought.

But as a matter of fact in markets, though monetary changes of price are incessant, yet general relations are constant; and in a former page we saw that in relation to articles which human industry can indefinitely multiply, and which it does so multiply for the hope of profit, and within a "nation" in the economical sense, — that is, a group of producers within which labor and capital freely circulate, —

these constant relations are fixed by the "cost of production." What then is this cost, accurately? It is in relation to this that we shall find the hypothesis as to fixed value of money especially useful. All other modes of dealing with the subject are apt to leave the mind of the reader somewhat dull and stupid, and to make him, though convinced at each step of the reasonings, not quite sure of the effect of the whole.

This cost of production, in a mature state of industry, and where there is a strict division of persons into capitalists, artisans, and laborers, is the cost at which it would "pay" a capitalist to produce a given product; and the word "pay" means that he must have his "outlay"—the money he has expended—returned to him, and that he must have, over and above, so much by way of profit—so much "to the good," as we commonly speak—as will induce him to make the production. Translated into more abstract language, you can say that the capitalist must be in possession, or have the means of possessing himself, of certain articles possessing exchangeable value; that those articles are parted with, or destroyed in making the product, and that he must have articles of equal exchangeable value returned to him by the exchange of his product, together with a profit. But though a most valuable way of speaking for some purposes, for those of common exposition this abstract way is inferior to the more concrete way.

A great deal of the indistinctness which often hovers round the subject arises because those who think of it do not enough trace the matter as it runs through the mind of the capitalist. In our modern production all depends on him: it is he who settles what undertakings shall be embarked in and what not; which things shall be made and which left unmade. The price at which a thing can be bought is the price at which the capitalist will undertake to lay it down; if you want to know why one thing

is cheap and another dear, you must analyze in each case the calculations of the capitalist.

The first and most obvious thing which a capitalist must do is, to pay his wages: labor — the muscular and mental force of man — is a main element in almost all kinds of production, and the principal one in many. But we must be careful not to imagine that this labor which the capitalist purchases is one thing: it is hardly even one *kind* of thing. The labor of a ploughman is distinct from that of a clerk; that of a clerk from that of an engine-driver; that of an engine-driver from that of a cabinet-maker: and so on without end. The difference between these various kinds of labor is in a great degree the consequence of acquired habit: each man is trained in his department, and in it therefore he acquires a skill. These various kinds of training go down to very low degrees,— to the "navvy," who just knows how to dig out plain earth; and run up to the most accomplished artisan,—the maker of astronomical instruments, say, who can turn out work of the finest and most minute accuracy, and to a great extent knows how he does it and how that accuracy is acquired. There is a common coarse sort of human nature which can be taken a certain way in any pursuit, but which will not go very far; and over and above that, there is a finer element which can only be taken in one direction, or some few directions for which it has an affinity, and which is often accompanied by an incompetence to go even the first step in many others. Out of these natures specifically inclined to it, each trade gets its best laborers; the capitalist in each line has to try the various sorts, if he can get them, and to pay higher for the finer sorts. I say, *if* he can get them; because a main key to the reason why industries are distributed apparently so capriciously over the face of the country is to be found in the power of being able to buy easily and cheaply *all* the kinds of labor which each kind of

trade wants. In a place where a trade has long been carried on, all these tend to accumulate: a family tradition carries them on from father to son, and the whole mind of the place comes to be full of it; the language of the district soon assumes that you know it, and those who do not are a kind of aliens. "As water" in all cases "comes to the river," so the place where a trade has long been carried on tends to attract those who by nature like that trade, and feel that they are fitted for it. Thus commerce, which being wholly of human creation one might have fancied to be very mutable, is really a thing most conservative; it will stay in a place for very many years which has given no natural facility to it,— often which seems to have interposed a difficulty. To get all the kinds of skill suitable for a trade in their proper proportions is a long task, requiring many years; a new place cannot have it for a long time, and an old place for a long time will be superior in this cardinal advantage.

One special kind of labor which almost every capitalist must have more or less of is what we call his "establishment"; that is, his head men, who transmit his orders or give them to his corresponding clerks, [and] his book-keeping clerks, who keep what we may call his "memory": and the result of their labors shows what has become of his capital, and whether he is getting or losing. In some trades, as in banking and some other distributive trades, this kind of charge is one of the greatest; and almost all people in a very large way of business have a large staff of confidential persons whom they know and who know them, and who work together with an efficiency — though often incessantly "having words" — which no casual gang suddenly collected can for an instant compete with.

Next, a capitalist must buy his "machines"; and there is no reason to take up time and space with saying how various and wonderful they are at the

present day, — everybody will remember that, without its being said. What is much more to our present purpose is, to say that outlay on wages has a different effect on the price of commodities from an outlay on machinery. If £100,000 is laid out during the year in wages, that sum must all be returned by the sale of the articles produced in the year; but that is not true of an outlay on machinery, — on the contrary, £100,000 laid out in machinery need not all come back so soon. The machinery will last for years; and the capitalist does not want to have the first outlay returned to him till the very end, when it is quite worn out. Money spent on wages is a lump sum, which the products of the year must return; money spent on machinery a sum repayable by terminable annuity, extending over all the years the machine lasts. Each cotton shirting must by its sale recoup the capitalist for the wages spent in making it; but it need only return to him a small fraction of the cost of the machinery by which it was made, because that machinery will go on making shirtings for many years, and it is the aggregate which must make the return to the capitalist, and not any one.

Machine-making, it is to be observed, is a trade which especially tends to adhere to particular places, because more than any other trade it requires the easy and cheap supply of the exact kind of skilled labor in the exact quantity in which it is wanted; and this you cannot have in a new place. A machine-making factory which would thrive at Birmingham would starve at the Land's End.

Next, a capitalist must mend his machinery; and this is the most conservative force of all. The number of subsidiary trades which any one great manufacture requires merely to keep its plant going is very large; and in out-of-the-way spots no one of them, of course, exists, — they only grow round the principal trade gradually, and as time goes on. And many of them are subsidiary to several trades. The

place, therefore, which has longest had possession of such trades has an incalculable advantage, as far as this item is concerned.

Next, the capitalist, having bought his machinery, must buy the power of moving that machinery. And this is a point on which very many people have no clear notions; there is a difficulty in comprehending the difference between the two, — a disposition to confound force and wheels. In the old times of water-mills and windmills, I am inclined to think that the distinction was clearer; it was then patent that the most elaborate machinery would not move unless there was some external force to push it: but the use of coal has rather mystified the matter, — people do not see the pushing power, and therefore they do not believe that it exists. A steam engine is so large and complex a thing that people in general have no real idea how it moves. The truth of course is, that the burning of the coal heats the water, that the heating of the water causes it to expand, that this expansion gives a "shove," and that all the rest of the machine only transmits and passes on that "shove." You must have something like this to start with — something that will produce a pressure — or you cannot move your machinery at all. I have known highly experienced men of business, however, who are very far from clear about this. In discussion as to the consequences of the extinction of our coal, nothing is more common than to hear it said, "Oh, then we must adopt new forms of machinery." You might as well try by improving and educating the mothers to continue a species without fathers: there is a certain motive "power" in nature which is as essential as any matter to be moved.

This element in the cost of production tends quite in the opposite way to the previous ones; it tends not to keep trade where it is, but to make it move. The best coal mines, the best sources of power of all kinds in each district, are soon appropriated and

used. The natural tendency of trade, as far as this element in the cost of production guides it, would be to move incessantly over the face of the world, always touching the best sources of power only, — the quickest water-courses, the most exposed sites for windmills, the best coal mines, — and never stopping to exhaust the second-rate sources.

Next, the capitalist must buy the materials which he is to work up with this power and this machinery; and the effect of this item too is just like the last, — it tends to migration. The principal materials of industry are the tissues of vegetables, the fleeces and skins of animals, and the products of mines; and commerce is forever hunting out the places at which such animals can be reared, such vegetables grown, and such minerals extracted. New places are constantly being discovered where these can be done; and manufactures, if not tied by the other items of cost, would be forever stimulated to move by this one.

Then the capitalist must rent the land on which his factory is built, or on which his business is carried on; and what the laws are by which this is regulated, we have seen.

Next, he must pay interest on as much of his capital as he finds it convenient to borrow, and as he can get the loan of; and this is a steady cause operating in favor of old countries, because capital has there accumulated and is cheap; whereas in new countries it is still scarce, and cannot be borrowed except at great cost, if at all. As commerce becomes involved and credit complex, more and more of business tends to be carried on with borrowed money; and the comparative cheapness of it in established places of industry is one of the reasons why trades stay there as they do, — why so many of them are stationary and so few migratory.

Lastly, in many cases, though not in all, the capitalist must make known the goodness — or at

least must allege the goodness — of his work. Advertising is a kind of outlay which to some extent is essential in all trades, and it takes different forms. A company which hires a showy shop front, a broker who is forever sending round trade circulars, are really advertising just as much as dealers who insert in the newspapers, puffs of their articles: the end in all cases is to sell something, and in the long run the buyer pays for it all.

I have been speaking as if all products were made or manufactured: common language has no apt expressions for the general ideas of political economy. There is no easy mode of describing all the processes by which all sorts of articles are changed by men from the state in which they are worth less into that in which they are worth more; the case of a manufacturer is the simplest case to the imagination, and I have therefore taken it as the standard. Besides it there are the breeding of animals, the growth of vegetables, and the extraction of minerals; but any one who has analyzed the outlay of the capitalist in manufactures will have no difficulty in doing so for the others, — *mutatis mutandis*, it all comes to the same thing, though the words of describing it differ. In all, the capitalist will have to pay wages; to buy co-operative instruments (animals included); to obtain a site; probably to borrow capital; probably to make known the value of his article. His outlay will be on these; and what he has over, after replacing these, is profit. The whole of business in great commercial countries is that of a replacement, with an addition, of capital; as a rule, the capitalists of a trade must have their capital returned to them with the profit of the country, or they will not continue in that trade.

II.

One result of these truths is, I think, to clear up the most abstruse discussion in which English political

economy has recently been engaged,—the discussion which Mr. Cairnes raised against Mr. Mill on the "cost of production." And this result is just of the kind which might be expected; for it is in the beginning of arguments that their difficulties are hidden, and any one who will really go back to that beginning will be sure to meet his reward. Let us look at the matter a little carefully.

When any article, say a steam engine, is in our modern state of industry produced by a capitalist maker, it is necessary to repay to that capitalist maker all which he has expended upon it: if it costs £500, and the current rate of profit be a 10 per cent. rate, he must have £550. His capital must be returned to him, and he must have the remuneration for that capital for the risk of losing it, for the trouble of managing it, and so on. But Mr. Mill takes his analysis further: he analyzes the cost of production into the "wages of labor" and the "profits of capital": and after speaking of the former, thus proceeds:—

"Thus far of labor or wages, as an element in cost of production. But in our analysis, in the First Book, of the requisites of production, we found that there is another necessary element in it besides labor. There is also capital; and this being the result of abstinence, the produce or its value must be sufficient to remunerate, not only all the labor required, but the abstinence of all the persons by whom the remuneration of the different classes of laborers was advanced. The return from abstinence is profit; and profit, we have also seen, is not exclusively the surplus remaining to the capitalist after he has been compensated for his outlay, but forms in most cases no unimportant part of the outlay itself. The flax spinner, part of whose expenses consists of the purchase of flax and of machinery, has had to pay, in their price, not only the wages of the labor by which the flax was grown and the machinery made, but the profits of the grower, the flax dresser, the miner, the iron founder, and the machine-maker. All these profits, together with those of the spinner himself, were again advanced by the weaver in the price of his material,—linen yarn; and along with them the profits of a fresh set of machine-makers, and of the

miners and iron workers who supplied them with their metallic material. All these advances form part of the cost of production of linen. Profits, therefore, as well as wages, enter into the cost of production which determines the value of the produce."*

But this reasoning assumes that all capital comes from "abstinence," whereas a great deal of it does not. What the capitalist in this case really hires is, the use of the past plant of the world, whatever its origin. Thus the steam-engine maker hires the use of a whole series of tools and things, going back to the first flint implements and the first tamed animals. In the first beginnings of that series — the link on which it all hangs — there was no relinquishment of any enjoyment; there was no such "abstaining" as Mr. Mill supposes, and therefore Mr. Mill's analysis fails. He takes us back into a hypothetical history which he does not prove, and which he could not prove, for it is not true.

Further, Mr. Mill's analysis supposes the present organization of industry — that in which the capitalist buys the force of the laborer and pays him wages — to be the one which began at the beginning. Mr. Mill says:—

"What the production of a thing costs to its producer or its series of producers is, the labor expended in producing it. If we consider as the producer the capitalist who makes the advances, the word 'labor' may be replaced by the word 'wages': what the produce costs to him is, the wages which he has had to pay. At the first glance, indeed, this seems to be only a part of his outlay; since he has not only paid wages to laborers, but has likewise provided them with tools, materials, and perhaps buildings. These tools, materials, and buildings, however, were produced by labor and capital; and their value, like that of the article to the production of which they are subservient, depends on cost of production, which again is resolvable into labor. The cost of production of broadcloth does not wholly consist in the wages of weavers, which alone are directly paid by the cloth manufacturer; it consists also of the wages of spinners and wool combers, and it may be added of shepherds, all of which the clothier has paid for in the

* "Political Economy," Book iii., Chap. iv., § 4.

price of yarn. It consists too of the wages of builders and brick-makers, which he has reimbursed in the contract price of erecting his factory. It partly consists of the wages of machine-makers, iron founders, and miners. And to these must be added the wages of the carriers who transported any of the means and appliances of the production to the place where they were to be used, and the product itself to the place where it is to be sold." *

This principle, as applied to existing societies, may seem very obvious; indeed, it is most commonly assumed in popular discussions, both as being true and as being the principle of English political economy. But nevertheless, most eminent political economists refuse to regard it as ultimate, and try to get behind it. And no doubt in one sense it is not ultimate: there are processes acting on value of which it does not take account. For example, the wages of similar labor tend — though slowly — to be equal in all employments; and it is contended that you ought not to say that the exchange value of an article has arrived at its "cost" value while the wages paid in its production are greater or less than those paid to similar laborers in other employments. Again, the wages of dissimilar kinds of labor bear, as a rule, some kind of proportion to one another (though the exceptions to this rule are in all societies many, and though some of them last for a very long time); and it is said that we have not arrived at the "cost" value of any article until, in the case of that article, the different species of labor are rewarded in the same proportion that they are in the case of other articles. And no doubt if we choose we may thus define "cost value"; we may say that it is not realized till these conditions are satisfied: but if we do we must go further, and regard "cost value" as an ideal limit, rather than as any actual thing at all. In truth, the conception of the universal influence of the capitalist employer is essentially modern. We have seen before that capital is scarce in new countries, that it moves slowly, and that the laborer and the capitalist

* "Political Economy," Book iii., Chap. iv., § 1.

are often one and the same ; there is no such separate outlay as Mr. Mill's analysis presumes and as our modern practice exhibits. On a large scale, no such thing is possible till a good available money exists in which wages can be paid ; and such a money did not begin till the human race had been working and laboring for many hundred years.

Mr. Mill's attempt to answer the question, "What is the cost of production which determines value?" by saying that it is the sum of the wages of labor and profits on abstinence since the beginning of history, fails therefore at both its cardinal points: for in the beginning of history there was much capital yielding profit which did not come from abstinence, and much labor which was not paid by wages ; and this capital and this labor were the seeds of all which now is, and must be reckoned in the list of things that made it, if we add up those things.

Nor do I think that Mr. Cairnes, most acute as he is, here as always, at all mends the matter. He says that Mr. Mill was wrong in adding up past wages and past profits so as to make a total "cost of production," for that neither wages nor profits are properly part of that cost at all. He tells us:—

"Of all ideas within the range of economic speculation, the two most profoundly opposed to each other are cost and the reward of cost, — the sacrifice incurred by man in productive industry, and the return made by nature to man upon that sacrifice. All industrial progress consists in altering the proportion between these two things ; in increasing the remuneration in relation to the cost, or in diminishing the cost in relation to the remuneration. Cost and remuneration are thus economic antitheses of each other ; so completely so, that a small cost and a large remuneration are exactly equivalent expressions. Now, in the analysis of cost of production which I have quoted, these two opposites are identified ; and cost, which is sacrifice, cost, which is what man pays to nature for her industrial rewards, is said to consist of wages and profits, — that is to say, of what nature yields to man in return for his industrial sacrifices. The theory thus in its simple statement confounds opposite facts and ideas ; and further examination will show that

it involves conclusions no less perplexed, and in conflict with doctrines the most received."*

But the "cost of production," in the sense in which that cost determines market value, means the "cost" to the person who brings it to that market. In England, at present, the capitalist pays the wages, and he will not do it unless he earns the profit. These pecuniary items are certainly elements in *price*, and "exchangeable value" is only an abstract word for a perfect price, — a price which would never alter by changes in the money medium, and changes in which, accordingly, would show accurately the changes in the buying power of things. The pecuniary remuneration to the laborer, and the pecuniary remuneration of the capitalist, seem to me to be essential ingredients in the permanent money price which is to pay them both; for that price must permanently be such as will so pay them, and so pay them adequately.

Secondly, I do not think that abstinence and labor, or the rewards of them, are the sole elements in the existing cost of production. There is a third, which I call the hire of the present plant, — of the existing productive things in the world. Suppose that a man goes into business with borrowed capital only: he will have to pay the "compensation" to abstinence, — that is, the interest on capital to the man who lends him the money, — and he will have likewise to hire laborers and pay them their wages. But besides this, he will have to hire machines to make his things. I say "hire," not "buy"; for as far as the "cost of production" goes, this word gives more readily the required idea. A capitalist who has bought his machine gets back his money by an annuity; in the price of each bale of goods which he sells he includes a fraction of that annuity: it is as if he hired the machine, and paid so much per bale

*"Some Leading Principles," Part i., Chap. iii. (page 50).

as a rent or royalty for using it. When he buys the machine he commutes this royalty for a sum down: but he must get it repaid him annually, for all that; and this repayment is so much to be added to the interest which he pays on his borrowed capital, and to what he pays in wages, — it is an outlay which is a compensation neither for abstinence nor labor.

Cairnes would probably have said that as all the machines so hired were produced once by abstinence and labor, the hire of them was really a compensation to that past abstinence and labor; but here historical investigation again helps us. We have seen that the existing producing things of the world are the growth of a long history; that they are the product of many things, and that they cannot be set down as the products of simple abstinence and simple labor. If you resort to a historical explanation, the first requirement is, that the history must be true; no hypothesis or set of abstractions can here help, — the appeal is to what has happened in matter of fact, and what is said to have thus happened never did so. And you cannot even confine such reasoning to somewhat developed states of society, for the very essence of this reasoning is to go back into the past and to assume that the cause of economical production has been uniform, — has always been the product of the same two stated agencies.

And not only are the real facts of the growth of wealth thus inconsistent with the analysis which both Mill and Cairnes give us of the "cost of production," but they are still more inconsistent with the analysis of that cost which was generally held by the preceding generation of English economists, and which is constantly to be found in the writings of Ricardo, — though what seems to me to be a truer view is, as I shall presently show, to be found there also. This older analysis considers that "labor" is the sole source of value, and that all things of the same price have been produced by an equal quantity

of "labor"; but this older theory is evidently more unlike the facts than either of the newer ones. We have seen that these were not true, because they assumed that two factors — labor and abstinence — were the sole sources of wealth; and *a fortiori* the older theory is untrue, for it assumes that a single factor — labor — has alone produced wealth.

III.

THE difference which remains over in the hands of the capitalist is his profit; and this is a most essential element in the cost of production, for everything in developed trade depends on him. Unless he brings an article to market it will not be brought, and he will not bring it unless he has enough to repay him for what he does; and what he does is the most intellectual part of wealth production and distribution.* He is to the rest of the people so engaged what the general is to the army: it is he who settles what work operatives shall do, what sums clerks shall add up, how the managing men shall be employed. Not only does he save his capital and does not eat it, not only does he risk his capital, but he manipulates his capital. It is common to speak of the intellectual part of profit as the "wages of superintending wisdom": you might as well call whist superintending the cards. A man who plays cards very ill will probably "play" his capital just as ill; the same kind of sagacity, the same observation, the same self-restraint are required in both. But though this is required of the capitalist, it is not all which is required; there is quite a different element besides. All business is in the nature of a game more or less difficult, and requires the same sort of faculties and same kind of attention as a game. But in most trades a capitalist has to govern others; a large employer of labor has to govern many men. He

* That is, of course, of wealth-production and wealth-distribution: a dash in the text makes the whole sentence meaningless there.— ED.

has not only to move his pawns, but to rule his pawns; the pieces with which he plays are of flesh and blood, and will not move unless they like: he has to manage that they shall like. And unless he is paid for all this, the article will not be made.

Ricardo was the first to give anything like this analysis of the cost of production. We have seen how imperfect, how confused, the analysis of Adam Smith was; nor was there any great step in the matter made between his time and Ricardo's. The subject was not accurately worked out.

The analysis of Ricardo was undoubtedly defective, and he got himself into a difficulty of language which perplexes his writings and puzzles half his readers. Bentham said that he "confounded 'cost' and 'value'"; and in fact, having satisfied himself that things of equal cost of production will in the long run exchange for one another, he came to speak of the effect as if it were the cause, and of the cause as if it were the effect. I do not think he actually confused the two in thought, but he often seems to do so. Not being a highly educated man, he had, as has been said, a curious difficulty in the use of abstract language; he is like a mathematician in whose work there are a good many small inaccuracies, but whose work is still in the main right. Of course such a mathematician is a very imperfect one: the essence of mathematics is accuracy. In the same way Ricardo is a very imperfect abstract writer: the essence of abstract writing is precision, and in his use of abstract words he is defective in precision. Still, the fault is of words only: when you come to examine the thought, you find that there was no obscurity in it, — that it was perfectly clear in his mind.

It is a much worse fault that he only incompletely seized the notion that in an advanced state of society, where the capitalist brings the labor and offers the article for sale, the cost to the capitalist

is that which regulates the value. No doubt, as we have seen, it is easy to imagine a simple society, where the laborers all support[ed] themselves, — a set of hunters and weavers and fishers, — where labor migrated from employment to employment just as one was better remunerated than another, and in which, labor being the sole cost of production (that is to say, the laborers owning their own food and using their own tools), it was this migration which adjusted exchangeable value to cost; but there is a much quicker adjustment when capital is movable and rapidly changes from employment to employment. What it costs the capitalist together with his profit settles the value. It does so, though the rate of wages for equal qualities of labor may be higher in one trade than another. As long as that is the case, the cost will be higher in the trade where wages are higher, and therefore the article produced will sell for more; in the end, labor will in most cases migrate from the badly paid to the well-paid employment, and then the labor in both will be equally remunerated, and the price so far as it depends on labor will be the same: but even before this, the cost of production to the capitalist will regulate the price just as much as it does afterwards.

Ricardo might more than any one else have been expected to point this out; for he had an infinitely better perception of the quickness with which capital moves than any previous economist, and of the way in which it moves.

"Whilst every man is free to employ his capital where he pleases, he will naturally seek for it that employment which is most advantageous; he will naturally be dissatisfied with a profit of 10 per cent., if by removing his capital he can obtain a profit of 15 per cent. This restless desire on the part of all the employers of stock, to quit a less profitable for a more advantageous business, has a strong tendency to equalize the rate of profits of all, or to fix them in such proportions as may, in the estimation of the parties, compensate for any advantage which one may have, or

may appear to have, over the other. It is perhaps very difficult to trace the steps by which this change is effected: it is probably effected by a manufacturer not absolutely changing his employment, but only lessening the quantity of capital he has in that employment. In all rich countries there is a number of men forming what is called 'the moneyed class'; these men are engaged in no trade, but live on the interest of their money, which is employed in discounting bills, or in loans to the more industrious part of the community. The bankers too employ a large capital on the same objects. The capital so employed forms a circulating capital of a large amount, and is employed, in larger or smaller proportions, by all the different trades of a country. There is perhaps no manufacturer, however rich, who limits his business to the extent that his own funds alone will allow; he has always some portion of this floating capital, increasing or diminishing according to the activity of the demand for his commodities. When the demand for silks increases and that for cloth diminishes, the clothier does not remove with his capital to the silk trade, but he dismisses some of his workmen, he discontinues his demand for the loan from bankers and moneyed men: while the case of the silk manufacturer is the reverse, — he wishes to employ more workmen, and thus his motive for borrowing is increased; he borrows more: and thus capital is transferred from one employment to another without the necessity of a manufacturer discontinuing his usual occupation. When we look to the markets of a large town, and observe how regularly they are supplied both with home and foreign commodities, in the quantity in which they are required, under all the circumstances of varying demand arising from the caprice of taste or a change in the amount of population, without often producing either the effects of a glut from a too abundant supply, or an enormously high price from the supply being unequal to the demand, we must confess that the principle which apportions capital to each trade in the precise amount that it is required, is more active than is generally supposed." *

From this passage it would have been expected that Ricardo would have said that in the state of industry which in this passage he was dealing with, the cost of production which determines the price was the outlay of the capitalist, *plus* his profit, and so have shown the subject in its true simplicity.

* Chap. iv.

But though in many passages he approaches to this clearness, though continually you seem to see the thought in his mind, he never quite utters it; you can nowhere find it in words. The difficulty of applying to real life the cost of production, when explained in any other sense, comes out in the following passage:—

"In speaking," says Ricardo, "however, of labor as being the foundation of all value, and the relative quantity of labor as almost exclusively determining the relative value of commodities, I must not be supposed to be inattentive to the different qualities of labor, and the difficulty of comparing an hour's or a day's labor in one employment with the same duration of labor in another. The estimation in which different qualities of labor are held, comes soon to be adjusted in the market with sufficient precision for all practical purposes, and depends much on the comparative skill of the laborer, and intensity of the labor performed. The scale, when once formed, is liable to little variation. If a day's labor of a working jeweler be more valuable than a day's labor of a common laborer, it has long ago been adjusted and placed in its proper position in the scale of value."*

And fifty years ago, when manufactures grew but slowly, and when the arts were comparatively stationary, this mode of speaking may not have been wholly incorrect,—at any rate was not perfectly false: but nowadays the different skill used in different employments varies incessantly; it tends to increase with every improvement in quality, it tends to diminish with every improvement in machinery. Even between the same employment at different times it is difficult to compare it, and between two different employments it is impossible to compare it. In a long time the circulation of labor from employment to employment no doubt brings about a rough and approximate equality: but this is only in a long time; it is a gradual and most incalculable operation. The cost of production would hardly in any practical sense determine price at all, if it only determined value after so many years and so irregularly. In

* Chap. i., § 2.

fact, capital travels far quicker than labor, and there is some approximate equality between the products of two equal and similarly circumstanced capitals; and cost of production, when analyzed properly, is a prompt and effective regulator of "value."

But though Ricardo did not see this, as it is easy to see it now, he saw more clearly than many people now do that a rise of wages does not entail a rise of prices. As yet I can only deal with the case of a money-mining country,—a country of gold and silver mines: whether the fact that money—that the precious metals are obtained by foreign trade, does or does not make a difference, will appear afterwards, but in the money-mining country nothing can be clearer. Nothing can change relative value except that which alters relative cost of production; what acts equally on all commodities will alter the exchangeable quality of none. If all equal capitals were spent in wages equally,—say if one-half of every £100 was always so spent in every trade, including money-mining,—a rise say of 20 per cent. would not affect values at all: it would tell on gold-mining, as well as on every other kind of production. "Hats," to take Ricardo's favorite article, would be produced at 20 per cent. more cost, but then sovereigns would be produced at 20 per cent. more cost also; and therefore there would be no more reason for raising the value of hats as against sovereigns than the value of sovereigns as against hats,—the cause on one side is equal to the cause on the other.

This is at present curiously neglected in our common discussions. So far from political economy having advanced on this point since Ricardo's time, it—at least the common exposition of it—has retrograded. In the incessant discussions of late years as to the effect of trades-unions, it is perpetually assumed that if these unions extended to all employments, and if they produced a rise of wages

in them all, they would certainly and necessarily produce a universal rise of prices; but the slightest thought would have shown that this rise, at least in a gold-mining country, would act on the gold as well as on the commodities exchanged for gold, and that the effect upon the one would counterbalance the effect upon the other.

Ricardo's conception of the cost of production was over-simplified; it left out part of the truth, and consequently gave an undue prominence to the other parts: but the slightest comparison between it and the ideas of Adam Smith will show how great is the advance which political economy has made between the two writers. Ricardo's is a first approximation to an exact science; Adam Smith's is but a set of popular conceptions,— always sensible, but often discordant.

IV.

But it will be asked, If in each trading country the trader must receive the rate of profit of the country, what is it which determines that rate of profit? and this is rather a long topic of inquiry.

For popular purposes, it is easy to say that the profit of a capitalist in any undertaking is that which remains after the cost of that undertaking has been satisfied; the outlay must be repaid, and what remains over is profit. But in an ordinary undertaking, say in making cotton twist, there is this difficulty: a great deal of the outlay is upon machines and raw material, which are the results of previous undertakings, and which must in the long run be valued at the outlay on these undertakings, *plus* the profit at the rate of the time and country; and this profit is exactly what we are in search of. The common trade facts do not give us that which we want to know in a sufficiently simple form.

Supposing one capitalist ordered the whole article from the beginning: suppose the country was one in

which cotton was grown, and suppose that the capitalist who grew it made all the necessary machines (including any preliminary ones necessary to make them),— it is evident that his outlay would be of one sort, *wages* only. He would have to deal exclusively with laborers, for he would go himself to the root of the matter, and would employ the results of no previous capitals. His outlay would then consist of wages only, and his profit would be the amount remaining to him when that outlay was recouped. He would sell his article, and his profit would be the price *minus* the wages paid.

This analogy represents the real facts much more accurately than would at first sight appear. Supposing the profits of all trades to be equal, it would represent them exactly. The manufacture of a consumable article is divided, say into a hundred undertakings, by various capitalists. If any one of these were — all things considered — more profitable than the others, capital would leave those others and would collect in it. The natural tide of capital from the less to the more remunerative enterprise makes the profits in each part of an entire manufacture equal; which is as much as to say that it makes the entire manufacture just what it would have been had one single capitalist ordered or managed the whole of it from the very beginning to the very end. As we have seen, this doctrine of the equality of profit is but an approximation; but we have also seen that it is a most useful approximation, and what are the corrections to be made in using it. Subject to these corrections, therefore, we can say that the profit on an article entirely made and manufactured in the same country is the price of the article *minus* the wages spent on it. But we must reserve an inquiry into the possible profit where foreign materials and machines are used; for there is no transfer hither and thither of capitals between nations, and no consequent equality in the returns on them. We

can only return to that case after examining the primitive simple one, where everything is made in the same country.

You say, I shall be told, that the profit is the selling price *minus* the outlay; but you do not tell us what is the selling price. Nor can it be told without seeing how money is obtained. The price of a thing is the money for which it exchanges; and you must consider the nature of it before you can know what that price will be.

The money of commerce is composed of the precious metals, gold and silver, — say for shortness, gold, which is a commodity like any other: it is raised in the same way as iron, and according to the same laws; the capitalist must have in it the same profit that he has in other trades, and no more. But the difference between it and other trades is, that there is no need to sell the article. A capitalist raises so much gold, after a certain outlay; he can take that gold to the mint, and the difference between it and the outlay is the profit. There is no haze about it, — no difficult words such as "price" and "value": it is a definite physical quantity, — 10,000 sovereigns were expended on the mine, and 11,000 came out, making a profit of 10 per cent. The standard rate of profit in money mining is the rate of profit in the least productive money mine that can keep itself at work: all other profits compare themselves with that, for money is the standard of comparison, the reckoning engine.

Suppose it took a third less labor and a third less machines to produce an ounce of gold: an ounce of gold will exchange for one-third less of other things; its buying power will be that much less; corn, cotton, and all other things, will exchange for so much more of it. The money price of mining machinery will rise, the outlay of money necessary to work mines will augment, and the return to it, though greater in quantity, will be identical in proportion, — will be the

same rate per cent. The gold mines which cannot pay that profit will be disused, just as old worn-out iron mines are disused, and from the same cause, — it no longer pays to work them. There will, however, be this difference: though the rate of profit in the gold trade will be the same, in other respects the trade will have changed; general prices will have altered. In consequence, more money will be necessary to circulate the same commodities, — to do the same business. The same moneyed capital in the gold trade will produce the same number of sovereigns as before; it will yield as much per cent. The change will be, that the same "moneyed capital" will buy less labor and fewer machines, and the number of sovereigns that make the profit, though the same, will buy less of other things.

At every particular value of a sovereign there are a certain number of sovereigns required to carry on the business of a country. If more than that number is supplied, their value — their buying power — will diminish, and the price of all other things measured against them will rise. The machinery and labor by which sovereigns are made are a part of those other things, and their price will rise too. The outlay on the production of sovereigns will augment, and there will be a discouragement to produce them. The price in "sovereigns" of all other articles will have risen, as well as the outlay on their production; the apparent profit in producing them will therefore be as before. But though the outlay on a given number of sovereigns has risen, they are in no way better than before. There will therefore be a diminution in the production of sovereigns, and the number in circulation will be reduced to that required at cost value to conduct the trade of the country.

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The money rate of wages is a case of "supply and demand," using those words in the sense in which they have been explained; that is, it is determined

by the amount of money which the owners of it wish to expend in labor, by the eagerness with which they want that labor, by the amount of labor in the market which wishes to sell itself for money, and by the eagerness with which the laborers desire that money. This, as we have seen, is peculiarly a case in which the market feelings of the two bodies of exchangers are carefully to be considered. If the laborers are in want, they must take whatever the capitalists offer them; if the capitalists are in want, they must buy the labor on the cheapest terms they can, but get it they must. And the capitalist is as likely, perhaps, to be in want as the laborer. It is true that the distress of the laborer is much more conspicuous, and that he advertises it; he goes about saying, "I am starving, and it is the tyranny of capital which is killing me." But it is also true that the capitalist is in danger of ruin, and that he conceals it: if he cannot complete contracts which he has made, if he has to stay out of a return from his business longer than he can afford, he is ruined. But he will never say this, because it may injure his credit and quicken the coming of the evil. He will lie awake with anxiety till his hair turns prematurely gray, and till deep lines of care form on his brow, but will say nothing. And it is necessary to insist on this now, because our current literature — some even of our gravest economical literature — is dangerously tainted with superficial sentiment: it speaks much of the sufferings of the working men which are seen, and little of those of the capitalist which are not seen; but the capitalist, being a higher and more thinking kind of man, is probably of more sensitive organization than the laborer, and pecuniary anxiety is a more racking thing than any physical kind of pain short of extreme hunger. The mental feelings of the capitalist must just as much be regarded as those of the laborer, in computing the rate at which the money of the one will be exchanged for the labor by the other.

The real remuneration of the laborer is of course not settled by this bargain. Money is of no use to him any more than to others, except for what it will fetch, — indeed, as his wants are more immediate he feels this truth more than most others; and of what use it will be, is settled by its purchasing power. This is again but a new case of supply and demand, in the full sense of those terms. If the laborer is needy and has nothing beforehand, he will not be able to make his money go so far, — he will be obliged to take anything which the shopkeeper will give him; at other times he, like other people, may buy the goods of a bankrupt, "going at a sacrifice." He is also at the mercy of the other causes which raise the price of the articles on which he spends his money. A short harvest will send up the price excessively, by diminishing the supply of food, which the laborer wants more than anything else in the world; the passage of an army through the district will just as much effect this, by introducing new mouths to be fed who take the food, with paying for it or without. The real remuneration of the laborer in commodities is settled by one case of ordinary exchange against money, just as the money price of that labor is settled by another.

It has indeed been contended that there is something special in the article "labor" which affects this matter. It is said that if "labor" is not sold on a certain day, — that is, if the laborer is idle, — that labor is lost in consequence; whereas "commodities" are permanent, and can be sold one day as well as another. But many commodities are, as we all know, very perishable, and are so without changing the principle on which their price is settled; and hiring a man and hiring a horse are obviously acts of the same species. The laws which settle monetary value are the same in the case of labor as in other cases.

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APPENDIX.

The account of the market price given in the text, though long, and though I trust complete enough for its purpose, is not complete, and I should like to add to it a little. Political economy tends to become unreal if it stands aloof from even the *minutiæ* of trading transactions.

First. It is assumed in the text that the person who proposes to sell an article is possessed of it, — is a "holder," as we say in market language; but nothing can be more untrue than to imagine that this is always so in markets. Many persons perpetually sell what they do not possess; and this great change, as is natural, makes other changes. The buyer's position is not indeed altered; very probably he neither cares nor knows whether the person proposing to deal with him does or does not possess the article: he thinks only whether the dealer will or will not be able to deliver it; if he gets it in time to satisfy the contract, that is all which he cares for. But the seller has a new point to think of: not holding the article himself, he must consider at what price he will be able to obtain it. This is by no means in all cases an easy matter. The Americans have invented a cant word for an organized mode of obstructing it: a "corner," in their language, is a gang of persons who, having heard that some one has need of a particular article, obtain possession of the whole supply of it in the market, and will only sell it to him at an excessive price. With the great articles of consumption this attempt is futile, — the supply of them is too large and too much divided; but with articles held by few dealers in small quantities, — like many securities of minor importance on the Stock Exchange, — such a plan is always possible and often profitable; and a person who sells what he has not got must reckon on the risk of it. This is one considerable change from the circumstances of ordinary bargains; and another is, that no one makes a sale of this sort to obtain the means of meeting a liability. In common business it often happens that a man must sell at a loss, because he has an "acceptance" to pay next day, and no other means of paying it; but selling that which you do not possess, and

which you must at once buy and pay for elsewhere, is of little use in such a strait. It may bring a percentage of profit, but the *corpus* of the capital will not be available for the discharge of pre-existing liabilities; it will be immediately paid out as part of the transaction which brought it in.

In this case, therefore, the first condition of the formula must be modified, and the early part of it will run: —

"A bargain will be struck when the seller thinks he cannot obtain more from the buyer with whom he is dealing, or from any other;

"When he thinks he can himself obtain the article at a less price, and is willing to take the trouble and incur the risk of attempting to do so."

And the rest will stand as in the text.

Secondly. There is a corresponding case in which the buyer has not the money, at least not nearly the whole of it, at the time he makes the bargain. In Stock Exchange transactions this is exceedingly common: many buyers cannot pay for the securities they purchase except by mortgaging those securities; many banks lend on them, taking a 10 or a 20 per cent. margin, as it may be. In the cotton and other produce markets there are similar loans: the buyer has only a fraction of the purchase money himself; he borrows the rest on the goods which are the subject-matter of the transaction in order to complete it. In this case, naturally, there are the two contrary peculiarities to the last: the buyer has to consider whether he thinks he will be able to borrow the money, and whether the terms on which he will borrow it are good enough to make the transaction worth his while. There is in this case no fear of his being "cornered," — at least, not in a large money market like the English: the voluntary operations of no gang, however powerful, would ever prevent the holder of good securities from obtaining money; but the involuntary circumstances of all dealers may prevent him. In a panic there may be no money to be obtained, and he may be ruined by being unable to complete his contract; and at a less excited moment, scarcity of money may easily raise the rate of interest to a point so high as to turn the profit he expects on the transaction into a loss. In consequence, the second half of the first condition must be changed into this: —

"When the buyer thinks he can borrow the requisite money, and when he is sufficiently desirous of the article to make him take the trouble and incur the risk of attempting to do so."

Till now we have been speaking only of what are called "legitimate" transactions, — bargains, that is, which are intended to be performed, and which mostly are performed; but there is another

great class of contracts which are not intended to be performed according to their terms, and which are not so performed. These are "time bargains," of which there are some in most markets, but of which the Stock Exchange is the great seat. It is as common as anything here that a man should buy £20,000, say, "Peruvians," for a few days only, never intending to pay for them and never intending to take them. The seller on his side understands that they are not meant either to be delivered or to be paid for. The real contract is different from the verbal one; it is, that on the day on which the bargain, according to its terms, is to be performed, — the account day, as it is called, — the price of the bargain is to be compared with the price of the day, and that the buyer is to receive the difference if the price of the day is the greater, and to pay the difference if the price of the bargain — the price at which he bought — is the greater. In plain English, if the price rises between the time of the purchase and the "settlement," the buyer is to have the difference; if it falls, the seller is to have it. The bargain is in fact a bet disguised as a sale: each party is to win if the event he "backs," happens, and to lose if it does not. In this case the bargain will be struck —

When the buyer thinks he cannot induce the seller to fix a less price;

When he thinks this price likely to be less than the price on the future day of settlement;

When he thinks the chance of the difference he will receive if his anticipation is right, worth the risk of that which he must pay if his anticipation is wrong;

When the seller cannot induce the buyer to name a greater price, and when he thinks just the contrary as to these comparative prices and their resulting difference.

The "bulls" are speculators of this kind who buy, and the "bears" speculators who sell; but the object of both is to gain the "difference," — the former being sanguine and thinking the price will rise, and the latter being gloomy and expecting it to fall. It curiously happens, I believe, that the common outside public are almost always "bulls," — that is, take a cheerful view; and that it is the inside or professional operator who expects things to go down. And of course the sanguine people are those who lose; the cool inside speculator lives on the folly of the outside world.

Time bargains are, more than any others, influenced by preceding bargains. When a stock is rising, many people will rush to bet that it will rise more; when it is sinking, not so many people, but still many people, will be eager to bet that it will fall further. People who wish to bet on one side or the other naturally choose

the side which is at the moment winning, unless they have a reason to the contrary; and many of these speculators seldom have much reason. In consequence, attempts to rig the market are more successful in this kind of business than in any other: a league of knowing speculators which can make the market rise a little will be sure to be imitated by a crowd of unknowing ones, and will be able to make money at their cost.

Of course it is possible to pursue these transactions upon a sound calculation; if a man has a real reason for thinking that a stock will ultimately rise very much, he may succeed by "time bargains" in it: but those who have a sound reason for what they do, and those who gain by it, are few in comparison with those who have only fancies and who lose.

There is, too, an obvious defect in the formula of the text: it treats "money" — meaning all kinds of purchasing power — as if they were the same; but in reality they are different. "Cash" on delivery is better than a sale on credit, or than the best bill at a long date. The ready-money price of a thing is in consequence always lower than the credit price; at least it is so when the delivery of the article is equally immediate in the two cases. On the Stock Exchange — in the "consol" market, for example — it is occasionally said that the "ready-money" price is greater than the price for the "account" (the account days are twice a month); but this only means that the stock is very scarce, and that in consequence it is much more convenient to deliver it a few days later than at once. The payment and the delivery are in both cases identical. Wherever there is a real sale on credit, the price is always higher than in a sale for cash, because the buyer loses the use of the money for a time; and the credit price is sometimes much greater, because the buyer may not be a man in much repute, and therefore the seller may be disposed to ask a high premium for placing confidence in him, and he may be obliged to pay it.

The use of the formula given in the text will, however, lead to no mistake on this ground when we know how to construe it. A credit price can at once be reduced to a cash price as soon as we know the time for which it was given, and the degree of trust reposed.

There are also two speculative difficulties which should be cleared away. It is often said that we ought to include in the term "supply," or whatever equivalent word we use, not merely the supply which is really in the market but that which is coming to it, — as it is phrased, the "prospective" supply, as well as the "actual"; but I think that this would be a mistake. In the first

place, it would be quite contrary to the ordinary phraseology of the markets; their language always distinguishes that which is on the spot as the supply *par excellence:* and it is always most unfortunate in an abstract theory to use a word in one sense, which those who are most concerned with and most practically skilled in the subject of that theory use in a different sense ; the consequent puzzles are incessant and important. And in this case the language of the market defines a vital distinction: there is a great difference between that part of the supply of a commodity which can, if its owners choose, be used to make good a contract, and that part which, from distance or incompleteness of growth or make, cannot in physical possibility be so used. The actual supply for the purpose of any bargain is that with which the bargain can be performed; this is what ordinary dealers would say they dealt in. The coming supply, near or distant, certain or uncertain, complete or incomplete, influences the opinions of dealers and their wishes; it makes them more or less anxious to keep or to sell the actual supply: but both in practical effect and in scientific conception the two are distinct.

It is also asked whether, when we say that "supply" influences price, we mean estimated supply or real supply. In the formula of the text, I have not used the word "supply," for fear of ambiguity ; but have been careful to say that "I speak of the actual quantity" of the article in the market. The effect of this is very great, independently of the estimate of it, because the dealers who hold it — especially those who hold most of it — are in general somewhat anxious to be rid of it. What each man holds, and what he has to sell, is a much more vital thing to him than that which others hold; a little addition to his own stock is apt to influence him much more than a great increase to the stock in the hands of others. It is the "actual supply" which is the first force in the market, because each bit of it acts on the holder of that bit, and mostly guides him more than anything else.

Of course, however, the "estimated" supply — the notion every dealer has about the amount held by every other dealer — also influences all transactions: it acts on the mental element, — on opinion and on desire; according as it is less or more, it makes the seller less or more likely to think the article is likely to fall, and less or more anxious to dispose of it. But the estimate of one man will differ from that of another, and the effect on one will be counteracted by the effect on the other; and we must not confound the chance results of these varying opinions with the steady desire of each dealer to dispose of his own article. In the language of the market, "supply" means real supply; and in discussions about markets, it is much the best to speak in the same way.

International Coinage.

INTERNATIONAL COINAGE.

THE ALLEGED AND THE REAL ADVANTAGES OF AN INTERNATIONAL COINAGE.

[From the *Economist*, Oct. 31, 1868.]

THE Report of the Decimal Coinage Commissioners is a very sensible, though not a very original document. Perhaps it was not possible that so many clever men of different kinds of minds would concur in anything remarkably new. On the main point submitted to them they have arrived at a sound conclusion: they were principally asked whether it was or was not wise to alter by twopence the value of the English sovereign in order to make it equivalent to a 25-franc piece, and they have reported that it would *not* be advisable. Taken alone and by itself, such a change would not be worth the trouble it must cost; a slight alteration in such matters often entails nine-tenths the cost of a great alteration, though it will not bring a tenth of the advantages. Instead, the Commissioners suggest that there shall be a new international congress, in which on account of its magnitude and difficulty the subject should be again discussed, especially with the object of investigating whether the English sovereign would not be on the whole the best basis for an international currency, and whether foreign nations could not be induced to agree to it as such. On this last point we have much doubt, as we shall hereafter explain; we fear any great change *by* all nations must be accompanied, in seeming at least, by an equality of cost

and difficulty *to* all nations. If any one nation is to retain its main coin, and all other nations are to take that coin, the world we fear would think, ineradicably think, such nation favored. But besides their decision the Commissioners have given us a vast mass of excellent information, which will enable those who wish to form a sound opinion to attain it without real difficulty. As yet in England this question has never advanced to a practical stage; it has been a favorite with philosophers, it has interested individual men of business, but it has not reached common persons. Now that we have a large mass of true information, easily accessible and easily intelligible, the public may begin to form a steady opinion.

What then are the alleged advantages of an international coinage? They may be roughly classed thus: first, those which concern the convenience of travelers; secondly, those which relate to the exchange and transmission of coin; thirdly, those which relate to statistics; and fourthly, those which are concerned with general trade. Either in this article or in a succeeding one we shall say a little on each of these.

As to the alleged convenience of travelers, we cannot think that now and in the policy of England it ought to have the slightest weight. No doubt cases can easily be imagined in which such a consideration would be most important: if every English county had a different coinage, the vexation to travelers would be unbearable. Twenty years ago each of the Swiss Cantons had actually such a separate coinage; and what was worse, the coins of the same name and much the same look had different values in adjoining cantons, — *batzen* were one thing here and another thing there. In this very evidence, Professor Leone Levi tells us that on returning to Italy, his native country, he has seen the use of monetary reform. Formerly each of the little Italian states had a currency of its own, — in the Middle Ages

sovereigns clung hard to the prerogative of coining, because in case of need they might ease their treasury by depreciating the standard; and on that account ancient Europe, as we may almost call it — the world before modern changes began — was incumbered with many petty coinages. But now this evil is much diminished: the progress is steady and rapid towards a few great nations and a few great currencies, and therefore travelers are inconvenienced very little; the difficulty which an Englishman finds in getting francs to pass in France is nothing. So long as countries are large and their inhabitants numerous, no one would wish to derange the many transactions of the millions that stay at home to facilitate a little the few transactions of the hundreds who go abroad: the good to be realized is not at all equal to the evil to be incurred.

Secondly: as to the exchanges, there is much the same objection, — those who send coin abroad are so much fewer than those who use it at home, the number of exchange transactions is so infinitely less than the number of interior transactions, that it would be extravagant to trouble what is so common in order to improve what is so rare. Some persons who have not much considered the subject, and who have been not unnaturally deceived by the mode in which exchange transactions are calculated and quoted, seem to imagine that if all the world had but one coin there would be no exchange business. They see that the French exchange is expressed by saying how many francs there are in a sovereign; they see that the Indian exchange is likewise quoted by saying how many pence and shillings amount to a rupee: and therefore they fancy that if there were one money in India, in France, and in England, no such calculations would be needed. But the principal matter would reappear in an altered form. An exchange calculation is really the cost of remitting money from one country to another; that cost is substantially the

same whether the country from which the money is exported and the country to which it is imported have the same currencies or different currencies. Australia and England have the same currencies; the sovereign is the main coin in both: but nevertheless there is an expense in remitting money to Australia, — the remitting banks make a charge for selling their drafts, and this is the common exchange calculation in a new shape. If France and America had the same currencies as England, it would still happen as now that bills on Paris or New York would be at a discount or a premium. The amount of money wishing to go eastward across the Atlantic, and the amount wishing to go westward, would then as now settle how much was to be paid in London for bills on New York, and how much was to be paid in New York for bills on London; the original element in exchange transactions — the remittance of money — would remain as now, and the two principal accessory difficulties would be just as great. In practical exchange business the rate of interest is to be considered, and the state of credit also: if you buy a bill at three months' date you lose a certain sum in interest (depending on the rate for the day), and you rely on the credit, more or less good, of the parties to the bill. These main items of exchange business are in its nature, and no currency change can alter them.

There is indeed a possibility of a slight economy in coining by a single international currency. If a man export bar gold to France, unless he can sell it on terms he thinks fit, he must take it to the French mint and have it coined: but if he exported the same sum in an international currency, he could use it at once; it would be already coined to his hand. This necessity of coining, sometimes at least, operates as a friction in exchange transactions: a man who takes bar gold or silver to be coined in all countries loses the interest of the money during the

whole process of coining, and in some he has to pay a charge besides; he therefore is not ready to export coin so soon as otherwise he would be: the premium on bills rises to a slightly greater height, and bullion does not flow quite so quickly from country to country.

These minor obstacles to exchange business would be cured by a single pervading currency, and the mere calculations would be easier, — the sums to be done would be fewer and less complicated: and perhaps an increase of intelligibility may make exchange business less of a mystic knowledge, — may augment the number of those fit for it, and so lower the cost to the public of sending money from place to place. But minor improvements, such as these, are not sufficient to justify us in paying the price at which they are to be bought. We cannot make every one change their monetary habits or their coins to save a few clerks and dealers a few sums, or even to make money flow in and out of London half an iota more easily, or the millionth of a farthing more cheaply. You must promise the mass of men more than that before they consent to undergo vast trouble for you.

The same may be said of statistical improvement. No doubt a common unit of value in all civilized countries would facilitate vastly every kind of monetary comparison. The comparative revenues, for example, of different countries would "read themselves"; you could compare the expenditure of the various countries of the world, not as now by tiresome calculation, but as easily as we compare the accounts of the Bank of England from week to week. No statistical improvement could be comparable. But ordinary people do not care as yet, and for an indefinite period to come are not likely to care, enough about statistical science to undergo themselves daily personal annoyance for it. The change of the current coin would *bore* most men much, and most men care little for philosophy.

Such are the minor, and in comparison of their price almost imaginary, advantages of an international currency; the real advantages — those which make it worth while to consider whether we ought not to aim at it — are to be found in the state of trade, and we shall next week describe them.

THE REAL ADVANTAGE OF AN INTERNATIONAL MEASURE OF ACCOUNT.

[From the *Economist*, Nov. 7, 1868.]

We last week explained that some of the alleged reasons for changing our coinage, and for using one which foreigners would use too, were not sound: the advantages were indisputable, but they were not worth the cost at which they would be purchased. This week we have to state the great advantages which make it well worth while to think whether we should not make a great effort to establish an international money; those who have paid most attention to it for the most part think that it is. The essential point in which an international money would help commerce is very plain: suppose that trade circulars were all expressed in a single currency, instead of being as now expressed in many currencies, would they not be far easier to understand? "I have before me," says Mr. Hendriks, the eminent actuary, "Morgan's British Trade Circular, which is a good example among the many trade circulars which are published. The amounts are there represented in pounds, shillings, and pence; for instance, we find sums like 44*s.* 6*d.* per cwt., 2*s.* 1½*d.* per stone." And illiterate merchants in foreign countries, not knowing our mode of reckoning, are in a perfect puzzle as to what they would get for their goods. Clever and knowing men can make the calculations, but ordinary men cannot. Our imports are liable to diminution because the mass of foreign traders do

not comprehend our *price language;* we have to pay the cost of their learning it. Some few know it (few, that is in comparison with the mass of men), and they make a kind of monopoly — a source of privileged irreducible profit — out of it.

Our exports suffer probably more. Mr. Behrens of Bradford, one of the most eminent authorities on the subject, observes: —

"One of the great advantages which we expect from the change of course would be the immensely greater facilities which would be afforded for international transactions, particularly in England. I might instance the case of a merchant in Rio wishing to send a cargo of coffee to Europe. Supposing that in Rio they had also joined the convention, and we had not, the Rio merchant would find perhaps by a London price list so much per ton quoted for coffee; of course he would have to go through a very elaborate calculation, and take all the risks of the exchanges into account. On the other hand, if he found that at Antwerp or Hamburg (supposing those places had joined the convention) the price of coffee was stated in the same currency, or in some multiple of it, as his own, and with the same weights and measures, he would make the calculation easily; he would say, 'The freight is so many centimes per pound or so many francs per kilogramme, the commission is so much, and all the charges to be added to it amount to so much per cent.' He would at once see the total amount, and then he would say, 'I will allow one or two per cent. for the risk of the exchanges, and I can at a glance see where I must send my coffee to.' And most likely he would prefer sending it to the Continent rather than to England. As I said before, the competition between the different nations is so great that already our exports of manufactured goods are more and more reduced to half-manufactured goods; the yarns which must be woven into pieces before they can be worn increase every year. Although I do not say that the goods themselves decrease, yet the yarns increase; which shows that the manufacturers on the Continent are very much on the alert, and produce more every year. There is therefore a great danger that if the slightest impediment be thrown in the way of English commerce, our Continental customers will soon cease to take even the yarns; and if they have greater facilities given to them as against ourselves by the use of the same money, they will import cotton direct, and not even take our cotton yarns in future."

And again, Mr. Behrens tells us: —

"I had an instance of the difficulty caused by the multiplicity of foreign coins, and that a painful one. I had to draw upon a place at which I did not know whether the ordinary currency was the Prussian thaler or the French franc, — the place was Luxemburg; the amount was £97. I indorsed the bill at the exchange in francs; the party upon whom it was drawn said, 'Prussian money is our legal tender, and I will not pay the bill except in Prussian money.' The conversion from francs into Prussian money, and then back into English money, cost me upon this £97, 45 francs."

That is to say, an exporter of foreign goods cannot tell at a glance what money he will be entitled to, nor in what form of currency he will be paid; a sort of uncertainty hovers over all the subject.

The real end is, that in every newspaper throughout the mercantile world, prices should be quoted in the same manner. Commerce has very many and very great natural difficulties: distance of place, difference of character, difference of speech, are irremovable impediments. We may conquer them, but we cannot remove them; nature made them, not man, and man cannot hope to foresee the time when they shall exist no longer. But the painful existence of real obstacles is the very reason why mankind should not invent artificial ones. We are incumbered in our commerce already; do not let us be more incumbered than we can help. But we voluntarily invent impediments if one set of us count in one fashion and the others count in different fashions.

Persons who look at the facts at a distance may fancy that this diversity of monetary expression is a minor difficulty; but in fact it is not conquered. English bankers are supposed to be — perhaps are — the most educated part of the English business world; yet how few ever look with care at the accounts of the Bank of France! An enormous increase of late years in the note circulation has happened without

their heeding it; except from some *translation* in a City article, they have not an idea how much bullion the Bank of France now holds; yet all English bankers know that after the amount of bullion in the Bank of England, one of the most imperative influences upon our money market is the bullion in the Bank of France. Of course all bankers *can* turn francs into pounds, and some think they *will;* but few ever do. If the accounts of the two great banks were rendered in identical language, they would be criticized with equal accuracy; but now in England the accounts of the Bank of France, in certain cases the most instructive and important, are altogether neglected.

In other trades we see the same: the diversity of monetary expression is an effectual bar to common commercial understanding. Unquestionably, great firms employ skilled clerks, who translate these difficulties — whether of Norway or Austria or India — very rapidly; but ordinary traders cannot keep such clerks, — their profits are not great enough, their business is not large enough. They cannot export to these countries of confusing currency, because they do not know really what their goods will fetch, — how many pounds, shillings, and sixpences their price will bring home.

No doubt certain skilled exporters know all this, and make a large profit on their knowledge: one of the most intelligent said before the Commission that an international money would be disadvantageous to him, because it would render unnecessary a kind of knowledge which he possessed but which merchants at large did not share. The *democracy* of trade, if we may so say, is excluded by the present monetary complexity; little men used to small transactions cannot grapple with it: and yet it is the lesson of all our recent legislation upon commerce that we must facilitate the transactions of the many, and leave to take care of themselves the transactions of

the few. The more traders are able to trade, the larger and the better will our commerce be.

But will the nation gain? If we ask the nation to make a great change, we must show that as a whole it will gain a great benefit, — not only that certain persons belonging to it will gain one. The answer is, that an increase of commerce *does* benefit every one. An augmentation of imports of course benefits the people, because they have greater facilities in buying what they want and consuming what they wish. An increase of exports too is a benefit not merely to the exporter but to the nation; for it cannot be permanent without an increase of imports, which the nation can use, and it employs in the most profitable manner labor and capital which would otherwise be spent in a way comparatively unprofitable.

At present too, in many cases, international transactions are managed by a rough calculation; which means a calculation favorable to the calculator, and upon which he charges a percentage. In the French book trade, for instance, a buyer in England has commonly to give twelve shillings for a book costing in Paris twelve francs. No one contends that such is the just exchange; but it is an easy exchange, by which no individual purchaser loses very much, and by which considerable traders probably derive considerable gains.

To sum up, an international money would enable smaller people to trade, and new unskilled people to trade; it would abolish a toll which the consumer pays, and remove an incumbrance which the merchant feels. There would be a gain to every one worth every one's making a certain sacrifice to reach. But this advantage cannot be reached without a large change. It involves what is not always seen, — not only an identity of certain coins, but an identity of the common money of account. You must make the monetary language of trade circulars identical, or you will not have effected your object;

you will not have made *quotations* identical, and without that you will not augment trade much, help little or untrained trades much, or benefit the consumer much. Unless you make a great change you will not achieve anything worth much cost, or that justifies inflicting a difficulty on the many.

How this change is to be effected so that it may gain most and cost least, we will immediately consider.

THE CONDITIONS WHICH AN INTERNATIONAL COINAGE SHOULD SATISFY, AND THE REASONS WHY NO EXISTING COINAGE FULFILLS THEM.

[From the *Economist*, Nov. 14, 1868.]

In the last two weeks we discussed the reasons which were alleged on behalf of an international currency; we showed that though some of the gains most loudly spoken of were either trifling or unreal, yet that one class of the gains — the gain to trade — was so real and so important that it would be well worth a great sacrifice to obtain it. If prices were quoted in the same terms in every newspaper in every country, trade would be easier and trade would be larger. But what sort of currency must this universal one be, and what are the difficulties that must be conquered before we can possess it?

Such a currency, to be fit for the present needs of commerce and to be on a level with economical theory, must satisfy three conditions.

First. It must be founded on a single standard, not on a double. This may seem at first an easy condition, but we shall soon see that many existing currencies do not satisfy it. Practically it comes to this, — that a contract to pay a sum of money shall be satisfied only by the payment of a specified portion of one known metal: if that metal is gold, then by so much gold; if that metal be silver, then by

so much silver. Under the contrary system — that of a double standard — the contract may be satisfied in two ways: the debtor has an alternative; he may pay either so much gold or so much silver as he likes, and therefore there are two chances for depreciation. Whichever metal declines in value the debtor is sure to select, and that metal so impaired the creditor must receive. One set of causes reduces or tends to reduce the value of gold, and so may injure the creditor; another one reduces or tends to reduce that of silver, and thus hurts the creditor also: no change tends to benefit him. If either gold or silver rise in value, he will not get it; his debtor has the option, — he will pay the metal which has *not* risen. A kind of mist floats over some minds: they fancy that by using a currency of two metals they evade the danger of the depreciation of either; but they really risk the depreciation of *both*, — the impaired metal will always be preferred because it *is* impaired, because it is cheaper.

Secondly. The new coinage to suit present commerce must have a high *gold unit:* the sums to be paid are large, and therefore the medium in which they are paid should be costly. Silver is the characteristic currency of early nations and poor nations: by comparison it is plentiful, and therefore cheap; the small amounts which early trade requires were best paid in it, and therefore it was used. But now large transactions require a *dear* paying medium: the more costly the unit, the fewer the pieces to be counted and the easier the use of the currency. The same principle applies to reckoning on paper, which is, though it may not seem so, really more important than paying by coin. The use of arithmetic applies not only to actual business but to contemplated business. If a merchant begins to think of exporting goods, he reckons what he must buy at and what he must sell at; whether he in fact export or not is an after matter, depending on the profit he finds

and the capital he has: but anyway he counts on paper, and the unit of account is therefore more important than the unit of coinage. The unit of account concerns all *possible* transactions, whether they are resolved upon or not; coin is only used in actual transactions, and not by any means in all those. A high unit of reckoning is of primary importance, now that people always think of trading largely; and the best way of attaining it is by selecting some costly gold coin and making it our unit.

A few years ago there was such a fear of the sudden depreciation of gold that nations would have hesitated to choose it for their money; some nations even which already used it, in fright abandoned it: but experience shows that the panic was excessive, and that the depreciation which gold is undergoing is too minute and too gradual to be very important. Very possibly if we selected silver, new mining discoveries might begin to reduce its value. The notion of a commodity whose cost is constant, and whose relative value to other articles does not alter, is imaginary. Monetary business, like all business, is rough; we must take the metal that suits best on the whole. The risks of depreciation being only what we see, we had best take gold because we can pay in it and reckon in it the easiest.

Thirdly. The new coinage must be a decimal coinage. Every new coinage probably will be so, and a system which is to include nations already having a decimal coinage *must* be so. There is of course no kind of superior naturalness in a decimal division: it is only more familiar to us because we have ten fingers; if we had twelve fingers, as some persons have had (and physiologists say the breed might have been preserved), a duodecimal division would have been equally natural. But we cannot change the human frame or reverse past history: our arithmetical system is a decimal system, and it is plainly good that our coinage system should be the same;

we should then count all money by tens, just as we reckon on paper all things by tens.

Fourthly. The new system must be one which will do no violence to national jealousies. It will not do for one nation to say to any other, still less to all others, "My coinage is better than yours; my trade is larger and my coinage better known than yours: therefore do you adopt my coinage and give up your own." Most nations — all great nations, perhaps — are too sensitive and too proud to bear such language; the desire for an international coinage is not an imperious desire; the advantages it promises are substantial and real, but they do not at once strike mankind. The mass of residents in every country will say, "We do not trade abroad, we do not travel abroad; we can use our native currency very well: why should we change it? why should we learn a new system? We do not care about foreign currencies." There is a great mass of stagnant selfishness in all nations which will oppose this improvement as well as all others: we must not reinforce that selfishness by wounded national pride. If we ask the mass of English people to take the French coinage, or the mass of French to take the English, we shall not prevail: the French will say, "We will not yield to England;" the English will say, "We will not yield to France." Any plan must be based on mutual concession; every one may hope to gain much, but every one must sacrifice something.

These four conditions, taken together, altogether forbid the idea of adopting as the international coinage any present coinage. In terms the last condition forbids it for reasons of policy; but the three first equally forbid it for economical and intrinsic reasons.

The French coinage, though widely propagated by the immense influence of France, is a bad coinage. It is a decimal coinage, and is so far good; but it is

based on a very low unit and uses a double standard, which is absurd. The history of the French coinage is a remarkable example of the rash application of an incomplete theory. The French revolutionary legislators found the old French coinage in a most depreciated condition. It had originally been based on the pound weight of silver; but by continual tampering the *livre*, representing that pound, had come to be worth only 10*d*. The old division had been into 20 sous of 12 deniers each, like our own; but as the French pound had come to be so very different from the English, the subordinate coins were utterly diverse in the two countries, and the French ones too small to be of any use. The revolutionary legislators saw one part of the evil and remedied it, — they abolished the old confused subsidiary coins, and introduced an easy decimal division; but they did not perceive the rest of the evil. They left the unit of account nearly unaltered; the new *franc* is substantially the old *livre*. They never thought that they were by their improvements entailing a burden on France. If they had introduced no change, it would have been easy to persuade France now to make a complete change, — to gain at once both a decimal system and a high unit would have been incontestably worth a great effort; but now that France has, by a great sacrifice, attained one of these conveniences, it is hard to ask her to make a second sacrifice to gain the other. The *bore* of the low unit affects the few more than the many, the rich more than the poor, the cultivated rather than the ignorant; those who by their *inertia* are hardest to move, are in fact those who would gain the least.

The American currency is in a condition yet more curious.

"On the recognition," says Mr. Ruggles, the American Commissioner at the Paris Congress, "by England, in 1783, of the political independence of the United States, their then existing political organization, 'The Congress of the Confederation,' deemed

it proper also to throw off the monetary yoke of pounds, shillings, pence, and farthings. On the 6th of July, 1785, this Continental Congress unanimously passed the memorable monetary ordinance reported by the 'grand committee of thirteen,' of which Rufus King, one of the wisest and most far-seeing of the statesmen of America, was a member. Not only did it omit in any way to recognize the pound, but it distinctly brought in and established the dollar as the permanent monetary unit of the United States. Its precise weight was fixed by a subsequent ordinance, passed on the 8th of August, 1786, which further provided for the issue of a gold coin of ten dollars, to bear the impress of the eagle, which imperial emblem had been selected in 1782, in view of the national sovereignty then clearly discerned in the future. What was far more important, the ordinance expressly provided that the dollar should be decimally divided."

Considering how many exchange sums have been caused by the difference between the two currencies, this expediency of throwing off the "yoke of the £" is dubious. In order to avoid a fancied subjection, America imposed on herself, and England too, a most real bondage of calculation. The unit selected — the dollar of 4*s.* 2*d.* — is far too low to be selected by other nations as the basis of a currency; and the effect of the sudden American innovation, as of the sudden French, has been to create in the world a currency of half-and-half merit, which has one merit, the merit of a decimal division, but is otherwise unfit for international adoption. And as every new coin — as every new international reckoning, at least — is a new evil, the former rashness both of France and America is a difficulty to themselves now. Both created something so good that nations who have it do not like to lose it, but also so bad that those who have it not do not wish to take it.

The English currency is not subject to the same defects, but it is still faulty. Even were it politically possible to ask several great nations to adopt exactly the coinage of any one, the English coinage would not be one which it would be economically advisable to choose. No doubt it contains the great

merit which the French and American currencies want: it has a high gold unit. No doubt also it has totally escaped the "besetting sin" of the double standard: the English may claim the discovery of the true principles on that matter. But then the English coinage is not decimal: it contains the old division of the pound, first into $\frac{1}{20}$th and then into $\frac{1}{12}$th, which belonged to the Middle Ages. You could not propose that any nation which does not possess it should adopt it as it stands. The contrast between the French currencies and the English is perhaps characteristic of the two countries. The French is a symmetrical embodiment of imperfect principles; the English a confused embodiment of the best principles. The French looks quite right till you have to examine and study it; the English looks quite wrong till you see what it really is, and what such things ought to be. The French has a good "manner" and a bad "meaning"; the English an excellent meaning but a wretched manner. The first sight sees what is good in France; the first sight does not see what is good in England.

The German, the Spanish, and the remaining currencies of the world need not for the present purpose be discussed: they have no claims to be put forward as universal currencies, and no one does so put them forward. The conclusion we come to is, that no existing coinage is fit as it stands for international uses; and this is really the conclusion which should have been expected,—the conditions of an international currency, as we have stated them, are complex, and are very little likely to have been satisfied in rude ages. The double standard itself, though absurd in theory, is, if we look at history, rather plausible. Silver was the old currency of Europe; gold a mere article of dealing and traffic. Silver is the best currency for early times because it is cheap, just as gold is the best currency for ripe ages because it is dear. Gradually there has been a

transition from the metal of early times to the metal of late times; but it is not possible to discard the metal of early times, — the small transactions in which it is used are as numerous as ever, perhaps more numerous than ever. The two metals must be kept in use together; but the true system, the English system, is in the last degree refined. It makes the dearer metal, gold, the standard, — uses gold alone in considerable payments; but it uses silver as a medium for small payments, and discards all notion of a real comparison of its value with the value of gold. Twenty shillings do not really make a £; the value is arbitrary and the quantity coined is arbitrary. Gold coinage circulates at its true value, and an artificial silver coinage circulates at an abnormal value because of its regulated quantity. Naturally it was long before this nice expedient was detected, and till then both metals circulated together at this equation or at that. The common-sense of mankind says, We want them both, and we must have them both; the arrangements were left to some few who said they understood them.

The high gold unit, again, is not wanted in early ages: people only want cheap things and small coins; a high "reckoning engine" is useless. Nor would a decimal coinage have been comprehensible. The Arabic numerals which we use have made 10 look like a line of nature; but in the Middle Ages, and before these numerals were used, people did not think so much of *ten*, — they thought most of halves and quarters, of multiples of 2 and 4. All our conditions have reference to the modern world, and were not imaginable in the old world; we must not therefore be surprised if we have to invent a new currency, and do not find a fit one ready. What that new one ought to be, we shall next week discuss.

THE PRACTICAL PROPOSALS FOR AN INTERNATIONAL COINAGE.

[From the *Economist*, Nov. 28, 1868.]

We have before considered the motives which require and the principles which should regulate an international coinage. We have now to examine the practical proposals that have been put forward: we must see how far they accord with the principles, and how far they would insure the promised advantages. Unfortunately, according to the conclusions of our last article, every system of international coinage must be incumbered with a great evil: no existing system of coinage is at all fit for universal adoption. Whatever new one is chosen, there must be a great change in our common modes of reckoning; and there is no difficulty greater than this

The most prominent proposal is that of the Congress of Paris, — to coin in this country and in others a 25-franc piece, which should circulate in all and be a legal tender in them all. The particular coin — a 25-franc piece — is chosen, because by mere accident a coin of nearly that value is at present in circulation in several very important states. The English sovereign differs by 2*d.* only from that value; in France, any multiple of five francs would be intelligible, and so in Italy and Switzerland; Spain has already a nearly equal coin; Austria and Sweden are ready to strike one. The Commissioners describe the proposal in words which on account of their importance it is best to have before us.

"The recommendations," they say, "which were made by the Paris Conference, with a view of introducing gold coins which should be common to all countries, are: —

"III. That all gold coins hereafter struck in any of the countries which are parties to the Convention should either be of the value of five francs or multiples of that sum.

"IV. That a gold coin of the value of 25 francs should be struck by such countries as prefer it, and be admitted as an international coin.

"The effect of these recommendations, if adopted, would be to make a gold coin of five francs the basis of the international currency, and to substitute the proposed coin of twenty-five francs in England for the sovereign, in the United States for the half-eagle, and we presume in Spain for the doblon. In Austria and in Sweden a coin of this value would also be struck.

	Grains.
"The Spanish doblon, or piece of ten escudos, contains of fine gold	116.487
The half-eagle,	116.100
The sovereign,	113.001
And the new coin of the value of twenty-five francs would contain	112.008

"As regards the coin of this country, the change therefore which would be required would be to diminish the quantity of fine gold contained in the sovereign by about a grain (or, more accurately, .993 of a grain). The diminution in value would be about 2*d.* (more accurately, 2.126*d.*) in the pound, equal to .88, or very nearly $\frac{9}{10}$ths per cent. The existing shilling, which is only a token coin, would remain in circulation, representing $\frac{1}{20}$th part of the new as it now does of the existing sovereign; and in like manner the sixpenny piece, the penny, halfpenny, and farthing would remain, representing the same parts of the new sovereign as they now do of the existing sovereign. The reduction of the value of the sovereign must practically involve that of the pound."

But the great objection to this plan is, that on the face of it it does not attain the object: a *coin* of twenty-five francs value is to be universal, but nothing else is to be universal. The object, as we showed, which it was desirable to attain was the identity of money of account; *quotations* were to be the same in different countries, — an English merchant taking up a French newspaper was to be able to understand the money, and a French merchant taking up an English one: but the proposal from Paris does not effect this. Accounts would not be kept identically abroad and at home after the change, any more than now. The French written money would still be francs and centimes; the 25-franc piece would be in it what the half-crown

is in the present English money of account, — it would be a circulating coin, but it would not be a calculating term. If an Englishman saw that the Bank of France had 1,162,665,670 francs in its till, he would have to divide by 25 to know how much in international money that was; and he can obtain this quite nearly enough for most purposes, and the number of our present sovereigns equivalent to that sum, by the very same division. The case is still worse with the subordinate divisions. If an Englishman sees that cotton is 102 francs 50 centimes at Havre, or wheat 36 francs 50 centimes, what is he the better for the international coin? He has a sum to work to turn the printed quotation into the new coin, and if he has a sum to work he may just as well remain as now; he can turn francs and centimes into the old money just as well as into the new money.

The inconvenience of changing the value of the sovereign would be very considerable: it would be such as it would be worth while to incur for a great object, but not such as it would be wise to incur for a small one. If we are to change our currency, let us so change it that we may be intelligible to foreigners, and that foreigners may be intelligible to us; to make a slight alteration would cost most of the price and not obtain most of the advantage.

A controversy of much delicacy has, however, been started: it is said that England does not now charge a seignorage on the coinage of gold, but that under the proposed system she might begin to do so. The difference between the new sovereign of twenty-five francs and the present sovereign is only 1 per cent.: we might charge 1 per cent. for coining the new one, and so keep the value unchanged; what was taken from the quantity might be added by the charge of the government. And if all nations were at once starting a new coinage, this theory would be sound. Nothing requires a government to coin

gratis: it is a matter of convenience whether they should or should not charge. Whatever charge a government makes, raises the value of the coin, just as an additional cost in the manufacture of gold plate raises the value of gold plate; sovereigns made gratis would not buy so much cloth or so much cotton as sovereigns made at a charge. If it were only necessary to compare coin with commodities, a charge of seignorage might easily be imposed; but in this case the precise object is, to compare coin with coin, not coin with commodities. English money is to be likened to French money, — the present sovereign is to be made equal to twenty-five francs: no seignorage can help in this. Coin changes against coin according to the bullion contents. "It is evident," as Sir John Lubbock well puts it, "that the new sovereign could not be equal in value both to the existing pound sterling and to twenty-five francs of the present French currency: if by the imposition of a mintage it is made equal to the former, no advantage will be effected; while if it is reduced to the value of the latter, the necessity for compensation will arise."

But it is hardly necessary to consider this refined expedient, except as a matter of principle and as showing what is possible and what is not possible in international coinage. The proposal of the Conference of Paris that France should coin a 25-franc piece and leave the rest of the French currency as it is, and that the English should alter their sovereign by 2*d.* and leave the rest of their currency as it is, must be rejected on plainer grounds. It does not give us a common money of account; it does not give us an entire common currency; it does not insure that quotations of price should be identical: it only provides a single circulating coin.

A second plan is that which the Coinage Commissioners themselves recommend, — the use of the English sovereign as an international coin; but it is

not easy to believe that foreign nations would be content with a plan so simple to us and so difficult to them. If the plan is to give us what we want, it must involve a complete abolition and total disuse of the entire Continental coinage; we shall keep our principal coin, but they will lose all their coins. A mere common coin, as we have seen, be it the sovereign or the 25-franc piece, is not in itself of primary use: what is requisite is a common language of commerce, — a single money of account. Now, to induce the French to reckon in sovereigns and to keep their ledgers in pounds sterling would be a most difficult task. It would be said that it was a stratagem of England to advance English interests; it would excite national jealousy and awaken inherited ill-will. No doubt the English pound is the most important unit of account in the whole commercial world; perhaps (though this is much more disputable) the sovereign is the most important coin in the world: but a common French peasant does not know this, and would not believe this; no reasoning would bring it home to his apprehension; in spite of all arguments, he would think he was yielding to an enemy and that he was being cheated by an enemy.

THE PRACTICAL PROPOSALS FOR AN INTERNATIONAL COINAGE.

[CONTINUATION OF PRECEDING ARTICLE.]

(From the *Economist*, Dec. 5, 1868.)

THE unit suggested for an international money most contrasted with the sovereign and the 25-franc piece is that proposed by M. Chevalier. These two suggestions are founded on the notion of adhering as far as possible to existing coins; but M. Chevalier discards that principle. He says in substance: — "If you take the 25-franc piece you will have the

same difficulty out of France as if you proposed a new unit, and if you take the sovereign you will have the same difficulty everywhere out of England: it is best to go back to principle and take the best unit, — the scientific unit. You will then have a sound reason in which all nations will concur; you will surmount the difficulty of asking one nation to concede to another; you will be better in theory, and you will not be worse in practice." But then comes the question, What is that best, that scientific unit? What is it that all nations will see to be inherently preferable? What is it that for its abstract merit they will be willing to choose?

To this M. Chevalier gives what we must call a French answer: he founds himself upon the metric system of weights and measures; and he alleges not only that this system is in practice more convenient, but also that it is in some way more perfect than other systems in science and theory, which indisputably it is not. There is *no* unit of weight or unit of measure in itself and by any intrinsic quality better than all other weights; whatever selection you make must be arbitrary. Six yards long means six times the length of a certain rod in London; six pounds means six times the weight of a certain standard solid in London. There is nothing essentially good in this weight or this length; it happens to be fixed upon, but different ones might have been fixed upon. The French *mètre* is "the 10,000,000th part of the quadrant of the meridian passing through France from Dunkirk to Frementara," — which is as arbitrary a length as could be found. The French unit of weight is the *gramme,* which is a "cubic *centimètre,* or the 100th part of a *mètre* of distilled water of the temperature of melting ice," — as arbitrary and even as *curious* a thing as can be imagined. The notion of most Frenchmen that there is something very scientific here is an error; it was an arbitrary choice like any other, as good [as] and no better than any other.

But it is upon the metric system that M. Chevalier grounds his coinage scheme. He justly says that originally the principal coin was a principal weight in some metal: the pound sterling was a *real* pound's weight of silver in the beginning; so was the *livre Tournois*, which down to the Revolution continued to be the great coin of old France. This is the simple notion of a "coin," — some simple weight of a precious metal, authenticated by government or in some way. M. Chevalier, with great learning and great acuteness, exemplifies this as in the Chinese system and in other systems; and he argues that because the original coin was a simple weight in some metal, so the new one should be too, — any fractions are an incurable defect. Then he objects to the 25-franc piece, because when written in the metric system of weights it appears as 0.32557 grammes, and the English sovereign it is also not possible to express neatly. But we cannot agree to this logic: it does not follow that the new coin ought to be a weight very simply expressible, because [the] oldest coins in their origin were very simply expressible. The notion of a coin began so; it could not else be made intelligible to barbarians: but we are not barbarians; we know what a coin is, well enough. We do not care what exact weight a sovereign is; we know it contains a certain weight of gold, because that gold is the source of its value, but we never in practice think about it. In fact, the sovereign is *not* easily expressible in English weights. An ounce troy coins into $3\frac{223}{480}$ sovereigns, or 480 ounces make 1869 sovereigns, and you cannot state it more easily; but no difficulty arises: we do not think of the origin of coins; we do not care what was the relation in the first times between simple weight and primary coin; we use our sovereigns and we do not care. We understand fractions well enough to be able to weigh great masses of sovereigns when we want. A simple equation between

the unit of weight and the unit of coinage may be a theoretical advantage, — a determining reason for choosing between two or more units equally convenient; but it is not a primary quality in such coins, it is not an essential requisite.

M. Chevalier's exact proposal is, that the new unit should be a piece of ten grammes weight; as he says, "once and a half the volume of a piece of twenty francs." But why *ten* grammes weight? Why not one gramme, since a gramme is the unit of weight? It seems a gramme is too small for a unit; you could not make a nice money by multiplying it and dividing it. But surely this shows plainly that the entire question is one of convenience and utility; that the "unit of weight" has no indefeasible title to be a "unit of money"; that we must judge whether it should be so by a comparison of that advantage with other advantages.

The real question is simple; it is only this: — Which is more important for a new international coin, — an easily expressible relation to the unit weight of the metric system, or an easily expressible relation to present coins and present moneys of account? M. Chevalier decides in favor of the former; but we cannot agree with him. We attach no special scientific value to the French metric system; we do not think it of primary importance that the unit of value should be a simple (though arbitrary) element of the unit of weight; we regard it as very important that the new coin should be easily expressible in old coins.

The last of the most remarkable systems which have been proposed for an international coin is one of singular ingenuity. It was proposed by the present Master of the Mint — one of the English representatives at the Congress of Paris — that ten francs should be taken as the unit of value, and that a gold piece of that value (it would be nearly 8*s.*) should be struck to represent it. The principal advantage

of this scheme is plain: those nations who now reckon in francs would be able after the change to reckon in francs; those who now use the French coinage — or, as we should now call it, the coinage of the International Convention — could continue to use it; the novelty is identical with a great reality. The exact scheme and the way it seems to have suggested itself at the Congress of Paris is thus described by the British delegates: —

"The renunciation of the principle of a currency based on a standard of silver seemed to imply and necessitate the adoption of a common unit of higher value than that at present prevailing in countries not possessing a gold standard, and the piece of five francs was that which, in spite of individual objections, found favor with the majority of the Commissioners.

"Exception was taken to it by some of the members for the practical reason of its insignificant dimensions, and upon the more theoretical ground that it does not perfectly harmonize with the decimal system.

"We shared this opinion, and were prepared to have suggested as preferable a ten-franc piece, which would not only be free from these drawbacks, but would be more likely to be acceptable in England, which is accustomed to the higher unit of the sovereign.

"A new British coin having the same quantity of gold as the ten-franc piece, with the same proportion of alloy, would be within ¾*d.* of 8*s.* in value. Such a piece could be legally introduced into circulation as an additional member of the present coinage, provided it was issued as a token coin for 8*s.* and made a legal tender to a limited amount only, such as £4 or ten pieces. It could have inscribed upon it '10 francs' in addition to its current value of '8*s.*' This coin would become the unit of computation, the new pound or metrical pound; or it might be made the tenth part of a new metrical pound, if a denomination of higher value were demanded. We would thus become possessed of an international coin.

"The scheme of coinage which it would be the means of suggesting is one resting upon the penny reduced four per cent. in value, and would include a silver piece of ten such pence, in addition to the gold piece of 100 pence. The ultimate adjustment of the European and American coinages contemplated would present: —

"In the French coinage:

"1 franc divided into 100 centimes;

"In the American:

"5 francs (dollar) divided into 100 cents;

"In the British:

"10 francs (gold florin, one metrical pound, or one-tenth of a metrical pound), divided into 100 pence; with the addition, if desired, of 100 francs (one metrical pound, £4 sterling), divided into 1,000 pence.

"Such a coin as the gold 8*s.* piece could be produced without expense, owing to the seignorage of ¾*d.* which it would yield as a token, and the piece could be made sufficiently distinctive by giving it a plain edge. For the issue of such a piece there is the precedent of the silver florin, which was devised to represent the pound and mil system, and to bring that system under the notice of the public. The 8*s.* piece proposed would represent the metrical system founded upon the penny, which has always been a rival with the former in general estimation, and which seems entitled to equal consideration at the hands of government. The issue of such a piece, while it brought the metrical system of coinage into notice, would not be conclusive as to the ultimate adoption of that system, but would leave it possible to advance in such a course, or to recede from it at any time without embarrassment."

As the delegates state their plan, it involves the immediate issue of an 8*s.* gold piece, which is to circulate with the present coins. But in this there would be much harm and no good: it would be very inconvenient to have at once in circulation, pieces so alike in appearance but so sensibly different in value as an 8*s.* gold piece and a 10*s.* gold piece; the cashiers of all banks would rebel against the puzzle, and in practice it would cause constant mistakes. The half-sovereign we must have, and so the 8*s.* piece would be unpopular as an introduction of the proposed coin; it would be a bad introduction. The 8*s.* piece would begin by creating blunders and causing plague; it would be itself unpopular, and make everything allied to it unpopular too.

But though the immediate issue of a ten-franc piece in England is out of the question, its adoption

as a basis for a universal money is by no means out of the question. There is indeed one objection of great magnitude to it, — of the greatest magnitude, to English ideas: the ten-franc piece is a very low unit. The tendency of nations is to augment the scale of their transactions; and the larger the transaction, the more convenient to have a high unit in terms of which to express it. The natural change is from a lower unit to a higher, and it is a going back in civilization to begin to count in 8*s.* pieces when we have been used to count in pounds sterling: the number of figures would be greater, and the reckoning would be more difficult. To this it is replied: first, that the reckoning would be in decimals, which for all paper calculations is indisputably easier, so that the increased facility by the improvement in the mode of calculation may be set off against the augmented difficulty from the degradation of the unit; secondly, that for very large calculations the new method may easily be made better than the old. As civilization augments and commerce extends, the sovereign may become an inconveniently small unit; indeed, even now the use of it often involves an inconvenient number of figures. But 100 francs or £4 might in the new system easily serve as a "*large-business* unit," and as a monetary statistical unit: it would perhaps be better than the sovereign for the last purpose, and as good as the sovereign for the first purpose.

In other respects the proposal to issue a ten-franc unit is faultless. It at once affords a basis for a universal money of account; prices could be everywhere quoted in it, just as they are now quoted in it throughout France and throughout the countries of the Convention. It thoroughly accomplishes the end if we can but make up our mind to the means.

There still remains a proposal suggested to the Commissioners, — that the 25-franc piece might be adopted in this country as a monetary unit, upon

condition that France and other countries adopted it as a monetary unit too; that we should decimalize upon that basis, if they would change their unit and decimalize upon it too. But the merits and demerits of this scheme must be discussed in another article.

THE RESULT OF THE INTERNATIONAL-COINAGE DISCUSSION.

[From the *Economist*, Dec. 19, 1868.]

THE proposal to establish a new unit of account of twenty-five francs has some plausibility at first sight: there is a coin very near to it in all the most important countries, — the Spanish doblon, the American half-eagle, the English sovereign are all very near to it; a decimal system of money and accounts based on this piece would be approximately intelligible wherever it is necessary. But here the merit of the scheme stops. Though like many non-French coins, it is identical with no coin; in Spain, in England, and in America there would be a slight change to be made, and in this matter the difficulty of making a change is not to be estimated by its arithmetical magnitude, — a small change may cause more difficulty than a great change. Even in France there is as yet no such coin in circulation; it has been proposed there, as a concession to foreign wishes, and especially to supposed English wishes, but it is not desired or thought of by the mass of the French. Its adoption as a unit will entail a change of every coin in the world and of every money of account in the world, and there is therefore no chance of its being chosen. It would be a contrivance to combine as many difficulties as possible and to puzzle as many people as possible.

A suggestion may, however, be founded on it. The great difficulty in all changes of coin is with

the smaller coins. This is the difficulty which has prevented and is long likely to prevent a decimalization of a coinage founded on the £. Twenty years ago and more the florin was struck as a first step to that scheme, and to prepare men's minds; but we are not a bit nearer that scheme than we then were. Mr. Gladstone told a deputation that he was by no means certain "we could get rid of the penny," and there the plan stuck. The mass of the community could not be persuaded to change the petty coins they use and reckon in; and so many tolls and charges — some belonging to private people — are assessed in the smaller coins, that we should be immersed in a complexity of compensations. No doubt it could be done, and for a great object ought to be done, but there would be endless difficulty in persuading the people to do it. On the contrary, if you retain the smaller coins, all other changes are in comparison easy: you do not require to change the habits of the mass of mankind; you address yourself to the users of valuable coins, who are in some degree educated; you can translate exactly each old sum, however small, into the coinage you propose; everybody could pay exactly what they had contracted to pay; no man's income would be menaced and no one's diminished. Now, a system can certainly be devised which would keep the English small money, and also the American small money: the plan of decimal coinage known as the "farthing plan" does this. We should have to change the sovereign to 1,000 farthings, or £1. 0*s.* 10*d.*; now, this is almost exactly the half-eagle of five dollars. Taking the dollar at 4*s.* 2*d.*, which by Act of Congress it is, the American cent is an English halfpenny; and the cent therefore could be retained in the United States as a paying coin, just as the halfpenny could be kept here. It would therefore be not only possible, it would for such a matter be even easy, to found a great *Anglo-Saxon* system of coins, — a system of coins which

would be common to both the great nations which speak the English language. And the two countries would not only obtain the advantage of uniformity, each of them would have a better coinage than it now has. America would have a high gold unit, and would reckon her vast debt and great taxation in units of suitable size; counting such large sums by dollars seems, and always must seem, like measuring their enormous territory by inches. England would have a decimal coinage and a decimal system of accounts which now she has not, and which as long as we keep the sovereign as our principal unit she is not at all likely to have.

No doubt it would be long before the French, and the other nations which have adopted their money, would change and adopt the Anglo-Saxon money. But still, the mercantile transactions of the English-speaking race are so much greater than those of any other race; a price current that an Anglo-Saxon can effectually deal with is a price current so much more important and so much more read than a price current which only the French and the copiers of French money can readily use, — that in the course of years it is very likely that the Anglo-Saxon money would become the *one* money. And even before then it might be and would be largely used as the principal money of *wholesale account:* every great firm in the world would quote prices in that great spreading and (so to say) oceanic money, as well as in its own local money. Besides, it must not be forgotten that Germany will have a currency to choose: none of her many currencies are suitable to modern commerce; and she ought to have — and will have, we may be sure, ere long — one uniform coinage and one single money of account. It is very likely, considering her great intercourse with America and England, that she might choose to select the money which we put forward rather than that which France puts forward. In that case there would be one Teutonic

money and one *Latin* money; the latter mostly confined to the West of Europe, and the former circulating through the world. Such a monetary state would be an immense improvement on the present. Yearly one nation after another would drop into the union which best suited it; and looking to the commercial activity of the Teutonic races, and the comparative torpor of the Latin races, no doubt the Teutonic money would be most frequently preferred. In this case as in most, the stronger would daily come to be stronger, and the weaker daily be—in comparison if not absolutely—weaker. Probably in the end the less coinage would merge in the greater; but at any rate it would be a great step to have but two moneys, and we could well make shift to do with that if we were sure, as we should be, that there never were to be any more.

The worst objection to such a plan is the present state of the American paper currency. The metallic dollar of 4*s.* 2*d.* is superseded by the paper greenback, worth a good third less; men buy in paper, not in gold, and sell for paper too. If the two countries adjusted their metallic currencies, they still would not have a monetary union, because one altogether rejects coin as a measure of value and the other adheres to it. Still, we may hope that the paper depreciation of America will be temporary; the other difficulties of a monetary union will take some time to settle, and in the mean time this one may settle itself.

It is true that even after this depreciation is cured, another difficulty would remain,—though by Act of Congress the dollar is valued at 4*s.* 2*d.*, in fact in real gold it is not so much; but after the immense alterations in the value of the dollar which the greenback system has introduced, it is not probable that the Americans would object to a slight change for the purpose of founding a monetary union

primarily with England, and gradually we may hope with much if not all the civilized world.

America has the casting vote in this matter. If she should in fact (as it has been said and suggested she would) join the existing monetary union, it would be useless to attempt to rival the currency of that union: it would then be supported by the principal nations of the Latin race, and by the second and the most augmenting nation of the Anglo-Saxon race; it would couple the *prestige* of the old Continent and that of the new. But as yet the people of the United States have never considered the "international-coinage" question any more than the people of England; when they do, it is probable that they would consider a union with England of greater importance than a union with the nations which have copied the French coinage,—her transactions with us are now far more than hers with them, and as we have before said, English-speaking business grows faster than any other business. So impressed was Mr. Chase with the advantage of a common money with England, that he proposed to Congress to adopt the English sovereign. But the change to a common union founded on the five-dollar piece must be far more pleasing to American sentiment than a change to the English sovereign; and as we have seen, it is better for us too, since any new international coinage must be decimal, and the decimal system founded on the £ involves so much interference with "penny business" that it probably could not be carried. Besides, it "stops the way" of all coinage improvement; not becoming itself more popular, but preventing Englishmen from attending to any scheme which might be popular and might be carried.

We suggest this scheme in no hostility to the ten-franc scheme; on the contrary, we think Messrs. Graham and Wilson, our Commissioners at Paris, who first suggested it, made an immense advance in

"*one*-currency" discussion. Before that there was no proposal which gave us one real money, one money of account. Before that the suggestions went to a common coin, — a five-franc or 25-franc coin; there was no plan at all which would enable prices to be quoted alike and bargains to be expressed alike. Nor is there any competing scheme now which could at once give us these benefits. The advocates have a strong position: they speak on behalf of a great monetary union; they say, "We have made a great sacrifice, we have abolished our old currencies; we have adopted a new currency: do you join with us, and change your currency as we have." It is hard to reply, "Oh, you have changed too fast; you have chosen a currency you should not have chosen: you must change again; you must make a third currency if we are to join you." Practically, the difficulty of inducing the present race of Frenchmen and French imitators to disuse the franc is insuperable. Generations must pass before they will think of it, much less do it. The "ten-franc" advocates have therefore the best of clients, — a client who will consent to "nothing"; they are able by the consistent force of obstinate multitudes to say, "If you will not have our union you shall have none, for we will not consent to any other. We have just 'built a new house': you may or may not come and live in it, but we cannot pull it down again and begin a third house to please you." What the answer to this is, we will next week show.

THE *REAL* FEASIBILITY OF ASSIMILATING THE ENGLISH AND THE AMERICAN CURRENCIES.

[From the *Economist*, Dec. 26, 1868.]

We last week said that nothing can exceed the ingenuity of the "ten-franc" scheme for international money; that it is more original than any other scheme; that it promises more than any other

scheme: but we fear that in practice there are too many objections to it. A responsible minister would hardly face Parliament with it.

First, it would alter the penny, and the penny is the unit of small payments. The indistinct manner in which this grave objection has been understood by some accomplished supporters of the plan is remarkable. Thus Mr. Leone Levi, on examination before the Commission, gave Lord Halifax, the chairman, these answers: —

"376. Do you think that such a complete revolution in the coinage as that would be well received in this country? — The penny would remain; and we must remember that when the discussion was carried on about the pound and mil scheme, a very large and preponderating number of persons were in favor of the maintenance of the penny above the sovereign, and more especially of the tenpenny scheme. The difference between the tenpenny scheme formerly advocated and my proposal is, that with mine you have a gold and international unit as the basis, whilst formerly that plan seemed to imply a silver unit, without introducing any uniformity with the coins of other countries.

"377. Would not the penny be altered too? — Not in reality, because the present penny is really worth ten centimes.

"378. One hundred pence are worth 8*s.* 4*d.*? — Yes, nominally.

"379. For that you would pay only 8*s.*? — Yes.

"380. There is therefore a difference of 4 per cent.? — Yes, the 25th part of every penny. What is contemplated is a unit of 100 pence; the relation it would bear to the present coin would of course be different.

"381. Your ten-franc piece would be 100 pence? — Yes, that is the basis.

"382. The ten-franc piece is equal to 8*s.*? — Yes, with the present penny.

"383. After the change? — No; then it will be worth 100 pence. I allow that there is some difficulty in this manner, arising from the slight change in the value of the penny; but the new ten-franc piece for the present should be issued as a token only. I consider it far easier to make that change in the penny than in the sovereign, which is the standard.

"384. I understand you to say that the penny would not be changed; would it not be changed? — Not in respect to its intrinsic value; in its relation to the present coinage it would

have to be. You could take the same penny as exists now, and count it at the rate of 100 to the 10 francs, because it is not worth more.

"385. Of course its intrinsic value is much below that? — Yes, that is what I mean.

"386. But the value for which the penny is current would be reduced? — Yes."

The truth obviously is, that all penny incomes would be taxed nearly 10*d.* in the £, and the owners would ask for compensation and must have compensation. An income tax so special and so sudden would not be borne silently. The owners of bridge tolls and ferries are not the main people; the whole system of railway carriage is based on penny charges. For example, the following are passenger charges: —

	First Class.		Second Class.		Third Class.	
	s.	*d.*	*s.*	*d.*	*s.*	*d.*
London to Birkenhead, . . .	33	6	25	0	16	1½
Birdbrook, ...	14	8	10	3	13	2
Beechington, . . .	15	0	10	6	5	10
Bishopstoke, . . .	14	6	10	6	6	1
Bishopstone, . . .	14	0	11	5	4	9
Bishop Stortford, . .	7	8	4	6	2	8

Again, the following rates are charged on a main line in Ireland, which is only an average specimen: —

RATES CHARGED.

		d.	
1.	Grain, ...	1¼	per ton per mile.
2.	Drink, ...	1¾	—
3.	Salt provisions, . . .	1¾	—
4.	Pitwood, ...	0¾	—
	Cut timber, . . .	1¼	—
5.	Artificial manure, . .	1¼	—
6.	Groceries, ...	2½	—
7.	Bale goods, including wool,	2½	—
8.	Bricks, tiles, slates, stone,	0¾	—
	Drain pipes, . . .	1¾	—
9.	Iron castings and machinery,	2½	—
	Iron agricultural implements,	4½	—
10.	Potatoes, ...	1¼	—
11.	Coal and coke, . .	¾*d.* to 1	—

These charges are often the highest the company can by law make; any minister who shall undertake to adjust them to a currency not expressible in pennies will have a hard task before him.

Secondly, a change to the French system of reckoning is a change that must be made at once. There can be no transition state; the two systems of reckoning cannot be used together. Neither pound, shilling, nor penny would have an exact equivalent in the new coinage or the new money of account. On a given day we must all take to francs and abandon shillings.

Some imagine that this interval can be bridged over by the issue of an introductory coin; it is suggested "that a gold coin of the value of ten francs (which is of less value than 8*s.* by about three-fourths [of a penny]) should be struck and issued as a token coin for 8*s.*, and be made legal tender up to £4." But no one would count or reckon in such a coin; no one would cash accounts in 8*s.* pieces; no one would quote prices in them, no one think in them. We have had for years the florin as an "introductory coinage" to the "pound and mil" scheme of decimals, but we are not nearer that scheme. No one writes in "florins" or talks in "florins"; they are pieces of 2*s.* and 24*d.*, and they are no more. The 8*s.* token would be equally neglected in thought, and equally useless as an introduction.

In the present state of the education of Englishmen the transition state is most important. In better educated parts of the world — in North Germany, for example — it is very likely that a sudden change in the modes of reckoning could be effected; but it is not so here. A great deal of counting both on paper and in the head is done by very illiterate people; especially by women, who can do things "their own way" very well, though they cannot explain what that way is, and though very often it is not easy to tell. Many a common tradesman who now keeps

or half-keeps books in our present money, could not keep them at all if he were obliged to keep them in any other money; he would get "bothered": pence, shillings, and sovereigns seem to him indispensable, and without them he cannot get on.

The change of book-keeping would be a greater difficulty because it would be coincident with a great change in prices. Almost all prices are expressed in pennies or fractions of a penny. Take the following list almost at random from our usual "price current":—

HIDES.

	s.	*d.*		*s.*	*d.*
Ox and Cow — B. A. and Montevideo, dry, per lb.,	0	6½	@	0	10
Do., and Rio Grande, salted,	0	5½		0	6¼
Brazil, dry,	0	7		0	9¾
Drysalted,	0	5		0	7½
Drysalted Mauritius,	0	6½		0	7¼
Rio, dry Rio Grande,	0	7		0	10
West Coast hides,	0	7		0	9
Cape, salted,	0	3½		0	6¼
Australian,	0	3¾		0	5½
New York,	0	3¾		0	4¼
East India,	0	6		1	1
Kips, Russia,	0	8		0	10½
South America horse, per hide,	6	6		12	0

INDIGO.

Bengal, per lb.,	1	1		9	11
Oude,	3	6		8	1
Madras,	1	0		7	1
Kurpah,	3	4		8	8
Manila,	4	6		8	0

These prices must be all changed, and most others too, at the same moment; one would be changed to the advantage of the seller, another to his disadvantage; and just then the retail sellers of the country would be required to adopt a new mode of account keeping. It would not be easy to many to know if they were gaining or losing, even if they reckoned in the old mode; and they would be quite at sea if they had to reckon in a new mode. The anxious country shopkeepers would be frantic, and the careless would be insolvent.

These are objections from "below," as it were, — from the world of small transactions; but there would be also great objection to the "ten-franc" plan from "above," — from the world of great transactions. It would be said, "For our purposes,* the movement is a retrograde movement. We have a unit, the sovereign, well suited to large business, and you wish us to go back and take less than half that unit. We now reckon in 20*s.* pieces, you want us to reckon in 8*s.* pieces."

For these reasons we fear we must reject the ten-franc plan. No scheme can be more ingenious, none more interesting; every one who has dwelt on the subject must have a partiality for it. But we do not know how to face its practical difficulties; with our present education and our present trading habits, we think they are invincible.

But none of these objections apply to the plan for a single currency which we might at once use, and the United States might at once use, and which Germany might soon join. That plan is to make the £ a 1,000 farthings, instead of 960; and its scale would run thus in our present money: —

	£	*s.*	*d.*
Unit	1	0	10
$\frac{1}{10}$	0	2	1
$\frac{1}{100}$	0	0	$2\frac{1}{2}$
$\frac{1}{1000}$	0	0	$0\frac{1}{4}$

Every sum in the old currency would be exactly representable in the new. There would be no difficulty in penny bridge or ferry tolls. The penny might continue to subsist as a coin, though it would not be a part of the decimal scale; just as the sou exists in France and is the basis of countless dealings, though it is neither the tenth nor the hundredth of a franc. It could at once be written in the new money of account, just as the sou can be at once

* I have rearranged the quotation marks here. As they stand in the *Economist* the last three words are meaningless. — Ed.

written in the present French money. All common dealings, all common quotations of prices, could go on just as well in pennies after the change as before; in *prices* there need be no change whatever; the new and the old would be exactly equivalent; they might be written differently on paper, but they would be the same number of pence and farthings.

What coins should be issued under the new system, and which of our present silver coins called in, would be a matter for very careful reflection; but whatever coins were selected, *accounts* might be kept for an indefinite time as now. If there were a piece of 2*s.* 1*d.*, for example, those who chose might deal with it as they now deal with the present half-crown; they might write it as 2*s.* 1*d.* in their accounts, with £ *s.* *d.* as at present. The main difference would be, that they would write the new principal coin, the *universal* as we might call it, £1 0*s.* 10*d.* Any one could learn it in a day, however ignorant and however stupid.

Again, no matter which of our coins were kept, it could be written at once in the new coinage. They are all multiples of the farthing, and whatever is a multiple of the farthing can at once go down on paper in the new currency.

The rules of reduction between the old and new systems of account would be the simplest possible. To turn the old currency into the new, the rule would be:—"Convert the sum given into farthings, put the decimal point after the third place from the right, and the result is the sum in the new currency." Thus, £185. 9*s.* 4¾*d.*:—

£	*s.*	*d.*
185	9	4¾
20		
3709		
12		
44512		
4		
178.051		

One figure less to write than our present currency. To change the new currency into the old, the rule would be:—"Treat the entire sum as farthings, and divide by 4, 12, and 20 as usual." To change 97.311 of new currency, we should only proceed:—

4) 97311

12) 24327 $\frac{3}{4}$

20) 2027 3

£101 7 $3\frac{3}{4}$

Again more figures to write than the new currency.

The new unit is so near the value of the old sovereign that it is impossible to say whether it is better or worse as a unit; and the trouble of adding 10*d.* to every £ in old accounts is not very arduous, besides that it would be facilitated by handy tables.

The Americans would have just the same facilities at the change, subject to the minute change to bring the value of the dollar to the Congress value of 4*s.* 2*d.* All their coins—their half-eagle, their dollar, their cent—would be exactly expressible in the new coinage. Their half-eagle—their five-dollar—would be the unit. They could keep their books as now and they could reckon as now if they liked; and they could change at once and on the instant adopt the new plan if they thought that more pleasant. Each American could judge for himself.

The real objection is, that after all this plan does not combine; it leaves us with two moneys: but if all the nations of the world gradually joined either the Latin coinage league or the Teutonic coinage league, trade would be very easy; and the amalgamation of these two might be left to a future and more educated age.

SOME ARTICLES

ON THE

DEPRECIATION OF SILVER,

AND ON

TOPICS CONNECTED WITH IT.

PREFACE.

I VENTURE to bring together these articles on the recent depreciation of silver, and on the recent exchanges with India, though I am well aware how incomplete a view they give of the complex subjects to which they relate, and how disagreeable to read a collection of such papers almost necessarily is. If I could, I would have rewritten the whole of them in a more systematic form; but I have no time or strength at my disposal for such a task, and I am obliged, therefore, to use this substitute. To elucidate some parts of the chain of reasoning, I have added the evidence which I gave on one or two points before Mr. Goschen's Committee on the Depreciation of Silver, last spring; but even so, there is much I should wish to say in addition, both in exposition and in defense of the opinions which I hold.

So far as the short experience which we have had goes, I think it confirms the view taken in these articles.

First, I consider that the rise in the price of silver, from 47*d.* last summer to 55¼*d.* now, shows the preceding great fall from 54⅞*d.* last February to be only a momentary accident in a new and weak market, and not the permanent effect of lasting causes.

Secondly, it has been proved that the demand for the countries which use silver as a currency is stimulated by its cheapness here and in America, and that this has carried off the late supply. China has taken the lead in so doing, mainly because she has

had a better and readier means of export; but sooner or later all other silver-moneyed countries will do so, according to their magnitude and opportunities.

And these are the two main propositions which I wish to establish.

If these are proved, the practical conclusion follows that it would be absurd to make any permanent changes in our Indian currency or taxation, while all the facts upon which such changes would be founded are changing so much and so rapidly. And though this conclusion does not need support, it is supported by our uncertainty as to the effect of the increased Home charges of our Indian government, — sometimes, for shortness, called the Indian "tribute," — which, in a way which I have tried to explain, complicates the whole subject.

The fertility of the new silver mines in America is not very elaborately examined in these articles, for even yet there are no sure data for us. But everything tends to show that the yield of these mines is likely to be far less than what was once thought, and the difficulty of obtaining exact data is an additional reason for being very slow to make any changes founded on a hypothesis as to the future price of silver. As yet no one can prove that the permanent value of silver — whether in relation to gold or in relation to commodities at large — will change so much as to render any alterations necessary.

[The Preface, as above written, was sent to the printers about the beginning of March. It is believed that Mr. Bagehot at one time contemplated making additions to it, but no memoranda have been left explanatory of his last intentions.

Economist Office, April, 1877.]

DEPRECIATION OF SILVER.

I.

THE LOW VALUE OF SILVER AND ITS EFFECT ON INDIA.

[From the *Economist* of Feb. 5, 1876.]

WHEN the great gold discoveries were made in Australia and California, most people expected that there would be a more or less rapid fall in the value of gold as compared with silver; but as a matter of fact the effect has been the reverse. The value of silver as compared with gold was 59¾*d.* per oz., or as 1 to 15.7, in 1849; it now is 54⅜*d.*, or as 1 to 17.1. Not only what the best judges expected has not happened, but the very contrary of it has happened.

And this has not been the result of any collateral cause; it is the direct consequence of the gold discoveries themselves. The effect of these discoveries has been a great improvement in the currencies of the world, which without them would not have been possible. The countries of great commerce and large transactions require a more valuable medium of exchange, bulk for bulk, than countries of petty trade and minor transactions: the labor of paying £1,000,000 in sovereigns is only a tenth of that of paying it in rupees, and therefore where millions have to be paid, sovereigns are a ten times better currency than rupees. Gold is much the best currency for rich nations of large trade; though silver does well enough, and is in some respects most suitable, for poor nations of little trade. But thirty

years ago it would not have been possible for the nations of great commerce to adopt this best currency: there would not have been gold enough obtainable. The supply from the mines was then barely sufficient to maintain the existing gold currencies: it would have been entirely insufficient for establishing new currencies on a large scale; no one then would ever have dreamed of proposing it. But as we all know, Germany has just now tried the experiment on a great scale; she is buying gold and selling off her silver: and in consequence, silver is cheaper than it has ever been before.

Probably, if there were gold enough for all the world, it would be best that there should be only a single standard of value throughout the world, and that one gold; but this is impossible. Some have doubted whether there is gold enough even for the nations which now intend to use it; and there certainly is not enough for all the world. Happily, the East has always been a country which had much silver, and for whose purposes silver was quite sufficient. The transactions of the East are small in comparison with those of the West, and therefore a bulky paying medium is not so inconvenient there as it would be here. Since economical history has been written, silver has been always sent from Europe to China, India, and the richer parts of the East, and never more so than in our own time. The payments of England in silver to India during the cotton famine were probably the greatest cash payments ever made in so short a time by one country to another. There is therefore in the end a certain market for the silver displaced from Europe: it will ultimately go, as the rest has gone, to the East, where it is the ancient and the best attainable paying medium.

But for the moment there is a difficulty in disposing of silver; there is no new sudden demand for it in the East. The case is not like that of the cotton famine: then we had incurred a large debt to India,

and we had to pay it in the only currency which she would take; we had to find an immense quantity of silver on a sudden, and France — owing to the peculiar operation of her double standard — found it for us. But now there is no such debt: the present problem is not to find the silver, but to find the use for the silver; and this is a slower process.

Sooner or later, however, the ordinary laws that govern foreign exchanges will do it for us. The consequence of the low value of silver is, that the rate of exchange is now 1*s.* 9¼*d.* per rupee (or less),— the lowest, or almost the lowest, ever known; and this operates as a direct discouragement to ship goods to India. These goods are paid for in rupees, and when the merchant wants to bring home those rupees to England, he finds that they do not go so far as they used to do; he has to pay much more for every £1,000 bill on England, and this extra cost destroys or diminishes his profit.

Secondly, the same state of the exchanges is a direct premium on sending goods from India to England: £1,000 received for those goods here will go further in buying bills on India than it used to do; in plain English, it will lay down more rupees at Calcutta in the same time than formerly, and this increase is so much extra profit. By this combination, therefore, — exports from India increasing on one hand, and imports into India diminishing on the other hand, — before long a large void will be created, which this silver, set free from Germany, will have to fill. The process will take time, but the effect is inevitable. The tendency of this great import of silver into India will be of course to raise prices, but the degree in which it will have that effect will depend on the degree in which it is counteracted by the causes which have intercepted its effect before: the hoarding habits of the people; the use of silver in ornaments (the ornaments being a sort of reserve fund to be sold in difficulty); the greater extension

of silver in rude districts, where barter is still much used; and the general increase of trade, which rising prices always tend to quicken and develop.

When this rise of prices has taken place, the encouragement to exports from and discouragement of imports into India will manifestly cease. The value of the rupee at Calcutta, as against bills on England, may remain as it is now; but the diminution of that value as compared with former times will be compensated by the greater number of rupees which the English exporter to India obtains for the goods which he sells there. The value of the £1,000 in London in purchasing bills payable on India in rupees may be as unusually great as now, if we compare it with the past; but there will be a corresponding difficulty in obtaining the £1,000 in London. The merchant in India will have to pay more for the goods which he sends to London, and in the end this loss will be equal to the other gain.

If new silver should still continue to come into the market, the same process must go on; the first step must be incessantly repeated. The value of the rupee must fall as against sterling money; instead of being 1*s.* 9*d.*, it may fall to 1*s.* 6*d.*: and then, *mutatis mutandis*, what we have just described as happening will happen again.

The effect, therefore, of the fall in the value of silver on the trade of India will be temporary only; but its effect on the financial position of the Indian government will continue as long as the fall lasts. The Indian revenue is received in silver, and therefore the less far silver goes in buying, the poorer will the Indian government be; and this is of more instant importance to the Indian government than almost any other, because its foreign payments exceed those of most governments, and those payments are made in gold. It has to pay interest in gold on a very large debt in England, to pay home salaries, maintain home depots, and buy English goods and

stores, all in gold; and the less valuable silver is in comparison with gold, the less effectual for these necessary purposes will the Indian revenue be.

On one species of its debt the Indian government will indeed not lose. The interest upon rupee paper is payable in rupees in Calcutta; and therefore the diminution in the value of the rupee is a loss to the creditor who receives, and not to the government which pays.

How long the fall in the value of silver will continue, no one can say. In the last resort, and taking great intervals of time into the reckoning, the relative value of gold and silver will be determined by their cost of production; but in the case of articles so durable, and so liable to be affected by political events like changes in coinage, it is difficult to say how long an average must be taken in order to exhibit distinctly this final result.

II.

THE REMEDIES FOR THE FALL IN SILVER.

[From the *Economist* of March 4, 1876.]

THE fall in the value of silver, of which we spoke weeks since, and which has attracted so much attention, proceeds from three causes: first, the actual increase of the production of silver, especially in America, — the extent of which is very considerable, as will be seen by the figures we give below; secondly, the amount of silver which has been set free by the German coinage operations, and has been sold here and elsewhere; and lastly, the perturbed state of men's minds which is consequent on these events. So large an increase of the supply makes dealers fear a still larger further increase; and therefore they do not wish to buy and do not care to hold. When markets are in this temper, speculations

are for the fall and not for the rise; and therefore there is just now a disposition to "bear" silver and to force its price down. Over and above the proper effect of the causes in operation, there is an additional effect consequent on apprehensive opinion.

The evils of the fall thus caused are two, and both of great importance. First, our English exporters to India and the East find their profits diminished or changed into a loss. They are paid in silver, which is the currency of those countries; but when they bring that silver home and turn it into gold, which is our currency, they find it is not worth nearly so much as it used to be, and this diminution is so much loss to them. In the presence of stagnant and unprofitable trade, such a sudden change for the worse is not easily borne; and its effect, as is usual in such cases, will be propagated through other trades. Secondly, the Indian revenue is received in silver; and the Indian government, which has to send some £15,000,000 home annually, for interest on its debt and other purposes, finds in the same way that the drafts from England on India, by which the remittance is effected, will not go as far as they used to do.

In the end, as we before showed, this fall in silver will work its own cure. Every country is bound to take any quantity of its own money in payment for debts due to it. As has been just explained, imports *into* India are no longer profitable; and by the converse operation of the same causes, exports *from* India have become more profitable than usual. The silver price of Indian commodities in India has not as yet risen much, though silver has fallen here as compared with gold, and there is therefore more profit than there was in exporting them: they can be bought with the same sum in silver, and that silver can be obtained more easily. The balance of trade will thus be, as the old writers used to count, constantly very favorable to India; silver will be

necessarily sent thither, and the prices there will rise. As far as commerce is concerned, at a certain time everything will be as it was before the fall began: the imports into India will be as profitable as before, because the silver prices in India will have risen as much as silver has fallen in relation to gold; and the exports from India, for the same reason turned the other way, will not be more profitable than usual. The equation of trade, as theoretical writers term it, will be as before. And if the Indian government were like most governments, its position also would not be altered, — as its taxes were paid in a medium of less value as compared with commodities, it must raise its taxes by an equivalent amount; but unhappily, the position of the Indian government is peculiar. The best portion of its revenue is derived from rent, and not from taxation; and that rent is fixed for stated periods — usually thirty years — in advance. On the £21,000,000 which the Indian government thus receives there will be a loss, which it will have to make good by some financial expedient; and as we well know, financial expedients are not so easy in India as they are in England. Still, such is the natural effect of these economical causes, and such the ultimate cure for the evils which are due to them.

As usual, however, other cures are suggested which, it is said, will be less painful and quicker. One is, that the Indian government should demonetize silver, as the Germans have been doing, and adopt a gold standard; but in this case the remedy would be worse than the disease. We all know what the Germans have had to do, and how painful its effect upon us has been: they have had to buy gold to substitute for that silver, and the result has been an unusual disturbance of the London market, with sometimes very high rates of discount; nor is the operation yet complete. But the effect of a similar operation in India upon us would be altogether

greater and more disturbing, because the Indian silver currency is so very much greater than the German. To get gold enough to supply the place of all this silver, the Indian government would have to buy constantly all the supplies from the gold mines for years, and so straiten incalculably the growing money markets of the world; and then what is the Indian government to do with the silver? The sales of the German government have greatly helped to send the price down already; the Indian sales would be on a much greater scale, and would come upon the market just when the supplies from the new American mines were arriving also. So much silver could scarcely be sold at all; the best result to the Indian government from this expedient would be far worse than anything which it is enduring now by letting things take their course, besides the disturbance to the London and other money markets.

Secondly, it is suggested that the German government should not sell any more silver, and so not reduce the price. But we may be sure that the German government will be guided, as in such a case it ought to be, by a regard to its own interest: when it thinks it best to sell, it will sell. Like any other holder of silver, it loses much interest by keeping very large sums; and looking to the possible magnitude of the American supply, it will probably not wish to incur for certain that great present loss at the risk also of a still further loss by depreciation. We cannot control the German government; it will act for its own interest, and it is best that it should.

Thirdly, it is said that our government should cease to draw bills on India; and our government is quite right in doing so at the present moment. There is, as we said before, at present in our judgment an apprehensive opinion which exaggerates the effect of the real causes at work; and also, as we are inclined to believe, speculation acting on and aggravating that opinion. In such a state of the market the Indian

government is quite right in doing as little as it can, and it would do ill to hurry to incur a loss which may be saved; but sooner or later it must bring the necessary sums home from India, and must bear whatever loss accompanies its so doing.

Fourthly, it is suggested by M. Cernuschi, the eminent French economist, that England, which was the first country to adopt the single gold standard, should take the initiative in abandoning it; that it should give up the present silver token currency, and instead "coin pounds sterling of silver in pieces of four shillings, and, concurrently with gold, put them into circulation." But the English government and nation will not easily be persuaded to abandon the monetary policy which they invented, and which on the whole has been so successful, just when all other nations are adopting it. The loss of profit on our present gold circulation, the cost of selling it and substituting a silver currency, are in themselves very considerable objections; it would take a very much greater evil than we or than India now feel from the present depreciation of silver, to outweigh them. The moment, too, would seem to the practical English sense most ill-chosen to choose to coin silver as a concurrent medium with gold, and therefore necessarily in a fixed relation with gold, just when silver is falling in value, and when we are not sure what its relation to gold will be. Monsieur Cernuschi speaks of the "universality of the $15\frac{1}{2}$": "Since 1803," he says, "the silver franc has weighed $15\frac{1}{2}$ francs of gold, and the silver marc now weighs $15\frac{1}{2}$ marcs of gold," and he would have us coin on this assumption and in this proportion. But the actual question is whether, in the face of the new and cheap supplies now brought from the American mines, this proportion can be maintained. Even if the best theoretical arguments could be urged for this proposal, it would for many years seem a paradox to our straightforward English minds, and they would be very slow to decide on adopting it.

But we think the theoretical argument is the other way; that it is in favor of our present English coinage, and not of M. Cernuschi's proposed substitute. We differ from him on a fundamental point of principle. He says that "the cost of production does not determine the value of gold and silver. That value is determined by two elements, — the employment and the quantity." But we say, on the other hand, that the value of gold and silver is determined by their cost of production, just like that of all other things; that in their case — as in all other cases — what is more cheaply produced than usual will be more plentifully produced than usual, and that the purchasing power in consequence will be no doubt less. Being durable articles, gold and silver are articles stable in general, though not always, in value as compared with other things, and a change in their cost of production does not so soon affect their value as a corresponding change in the cost of other commodities affects theirs; but the delay does not impair the principle, — in the end its effects will come.

The same causes which regulate the value of gold and silver as respects other things determine, as we believe, their value relatively to each other; and therefore as the circumstances of production of both are constantly changing, it is contrary to principle to make or attempt to make by law a fixed equation between them. So far, therefore, from M. Cernuschi's proposal being recommended by abstract argument, we think such argument forbids it; as well as its unlikely look, which for a long time will have as much or more effect on most English minds than any argument.

Lastly, M. Cernuschi recommends that Germany and Holland, which are in the course of demonetizing their silver, though at very different stages, should carefully consider before they go any further; and we do not feel able to say what effect this present fall in the price of silver should have on their present

plans. All changes in currency are delicate things, and we quite admit — indeed, we have often before maintained — that this is a particularly delicate one.

But these are considerations for foreign governments only. For our own government and that of British India, we believe there is no other policy possible except to leave the ordinary economical causes to operate; to suffer the present evil and to await the ultimate cure.

ESTIMATE OF SILVER PRODUCT OF THE UNITED STATES.

(Converting the dollars into sterling at 4*s.* each.)

	£
From 1849 to 1858, £10,000 per annum,	100,000
1859,	20,000
1860,	30,000
1861,	400,000
1862,	900,000
1863,	1,700,000
1864,	2,200,000
1865,	2,250,000
1866,	2,000,000
1867,	2,700,000
1868,	2,400,000
1869,	2,400,000
1870,	3,200,000
1871,	4,600,000
1872,	5,750,000
1873,	7,150,000
1874, (about)	7,000,000

The above figures are taken from the Reports of the United States Director of the Mint.

III.

FURTHER SUGGESTIONS ON THE FALL IN SILVER.

[From the *Economist* of March 11, 1876.]

THE grave difficulties which the Indian government finds in consequence of the fall in silver, and the much graver ones which it has to apprehend if that fall goes further and further, have naturally led to various suggestions, two of which are important enough to deserve notice.

First, it has been suggested that the Indian government should compel the ryots to pay the land revenue in gold at a fixed rate of exchange, say ten rupees to the sovereign; and it has been thought we shall so obtain most of the advantages of the demonetization of silver, without any of the disadvantages. But this we believe to be a mistake.

The measure, in the first place, would augment the depreciation of silver as compared with gold. Silver is at present the medium in which the land revenue is paid; if it is excluded from that class of payments and gold substituted, the rejected metal will fall and the adopted one rise in comparative value. The ryot who has silver ready to pay his land tax, finding that silver useless, must exchange it for gold; and an incessant series of such transactions would augment the depreciation which is complained of.

Secondly, the ryot would complain, and justly, of breach of contract: the government agreed with him to take so much silver for so many years, but now in effect it says it must have so much more silver. Suppose the silver rupee were only equal to 1*s.* 8*d.* in gold, and you make him find gold at 2*s.* a rupee; this is equal to an addition of one-sixth* to his taxation, and this will be a great hardship. If indeed the prices which the ryot gets for his commodities in silver had risen, he would be benefited as much as he lost, but as yet this is not so: the effect upon the relation of silver to gold has been much quicker than that upon the silver prices of miscellaneous commodities, and it would be a severe tyranny and real breach of faith to increase the stated land tax upon the ryot when his means of paying that tax had not been augmented.

Thirdly, the Indian creditors of the government, who are paid in silver, would say that their contract ought to be put on the same footing as the ryot's contract; that as he is to pay in gold at a fixed

*An obvious slip for "one-fifth." — Ed.

rate, so ought they to be paid. And their case will be stronger because, as we have seen, the depreciation of silver will be increased by this action of the government; and therefore its creditors may justly claim not to suffer by that which is — in part at least — the act of their own debtor.

Fourthly, the officials of the Indian government will at once say that they ought to be paid in gold too, at a fixed rate. And there would be a real claim to it as far as the English officials are concerned, for they are in much the same position as the government: they have to make large remittances to England for the investments of their savings, and often for the maintenance of their families. The prospect of making these savings has very much induced them to go to India; and therefore it would be unfair by any act of government materially to lessen their power of making them.

Other objections might be urged; but these are, we think, enough to show that the plan cannot be adopted.

The second scheme is even less plausible; indeed, we notice it rather because it has been spoken of in the market than for any merit it has. It is, that the English government should abstain from drawing on India, and should negotiate a loan in London. But this would only augment the evil; for the interest on the new loan would have to be paid in gold, and would be so much more if the gold was to be bought by the Indian government in depreciated silver.

In so far as the evil is real, there is, as we before showed, nothing to be done, except to endure the evil for the present, and to have confidence that the slow action of economical causes will in the end cure it. How far the present apprehensions are well grounded, and in what proportion on the contrary exaggerated, it would be as yet very premature to give an opinion.

IV.

THE EFFECTS OF THE RESUMPTION OF SPECIE PAYMENTS IN FRANCE ON THE PRICE OF SILVER.

[From the *Economist* of March 18, 1876.]

THE increased supply of silver from the American mines, the amount of it thrown on the market by the coinage operations of Germany, and the consequent fall in its value as compared with gold, have all been much discussed; but there is another event which will have a great effect on the matter, and which must sooner or later happen, that has not received at all equal attention,—viz., the resumption of specie payments by the Bank of France. The result of this, unless a change in the French coinage law is made, will be, we think, considerably to raise the price of silver as compared with gold, just as the result of the other causes which have been mentioned has been considerably to lower it.

Our older readers, and those of our younger ones who have followed the history of the London money market, will remember the exchange in 1860 of £2,000,000 of silver by the Bank of France for £2,000,000 of gold with the Bank of England, and the interest which it excited. We then explained what had happened, and the reason for it:—

> Why then do the Bank of France desire this arrangement? According to their own views, it was from no uneasiness as to their position. Notwithstanding the diminution in their reserve of bullion, they believe that they need feel no anxiety. By their last return their liabilities were:—
>
> | | £ |
> |---|---|
> | Notes in circulation, ... | 30,296,520 |
> | Deposits, etc., ... | 15,176,102 |
> | Total, ... | 45,472,622 |
>
> and their reserve was more than £17,000,000, and they consider that this is amply sufficient.

The difficulty of the Bank of France, it is said, is not the amount of bullion they hold, but the nature of that bullion. In their seventeen millions, the proportions are in round numbers: —

	£
Gold,	4,000,000
Silver,	13,000,000
Total,	17,000,000

And under the French currency laws this is not satisfactory. The Bank of France, for very sufficient reasons, prefer discharging their liabilities in gold instead of in silver. If they were to pay a note-holder £1,000 in silver, he could immediately sell the silver in the market for gold, and gain a substantial premium by the transaction; accordingly, the managers of the Bank of France apprehend that if they began to discharge their liabilities in silver, there would be a run upon them immediately for the sake of this premium. "If every note-holder knew that he could obtain an appreciable percentage on his note by getting it changed, depend on it," they say, "he would get it changed. The same causes which have drained the rest of France of silver (except for the smallest purposes, and of insufficient quantities even for those purposes) would begin to act upon us also; in a short time we should be drained of the whole of our thirteen millions of silver." And this, they say, is the reason for their proposing this anomalous arrangement to the directors of the Bank of England.

One remark must occur to every one when he hears this reasoning; it is the remark that no bank ever ought to be in this position. There must be some fault somewhere; there must either be bad management or bad legislation: there must be some peculiar error, or there could hardly be so peculiar a perplexity. For what is the allegation? The Bank of France say, "We have a large reserve, but it is not the kind of reserve we want. It is in the wrong metal; it is not gold, but silver." The alternative is irresistible that either the directors of the Bank have themselves made an error in hoarding a reserve in the wrong metal, or that circumstances beyond their power have forced upon them a hoard which they find they cannot use. They have a useless reserve, they themselves tell us: either, therefore, they have voluntarily selected it, — in which case they are to blame; or it has, by an unfortunate necessity, been forced upon them, — in which case they are not to blame.

Nor is this the only remark which must immediately be made; there is another very obvious but very important one. This useless

reserve is a misfortune not to the Bank of France only, not to the French only, but to us also, to Europe, and to the whole monetary world. We have thirteen millions sterling thus locked away in a great banking establishment, which does not dare to use any part of that sum for fear it may be deprived of all of it; and we have all been sufferers in consequence. The French demand for gold has been disturbing us for several weeks.

In truth the entire difficulty is caused by the French currency laws. There has been a question whether there is a double standard of value in France, and we will not, therefore, use the phrase; but there is indisputably a *double paying medium.* Both gold and silver circulate in France; both are legal tenders to any amount: and there is a fixed relation between them. A certain quantity of silver by law will pay a debt of 1,000 francs, and a certain quantity of gold will pay it also. One effect of this twofold currency has been often pointed out: the metal which is relatively depreciated will come into exclusive use; people will pay their debts in the least valuable metal, not in the most valuable,—in the medium which they can obtain *most* easily, not in the medium which they obtain *less* easily. But we have now to remark a different effect: *some* of the holders of the more valuable metal may be in a difficulty; if they are bound to pay either the less or the more valuable metal to their creditors, and they have not the former, they must use the latter. In consequence, in a country where two metals are a paying medium, those bankers who store up either metal for the necessary purposes of their business run a great risk. If it increases in value, there may be a run upon them, not because their credit is impaired, but because the metal they have chosen is desired.*

And the same cause will act on the Bank of France as soon as it resumes specie payments. The Bank of France holds now over £70,000,000 in the precious metals, and it is known that gold preponderates largely. Roughly, it is said that the proportions are—

	£
Gold,	50,000,000
Silver,	20,000,000
Total,	70,000,000

*See *Economist,* Nov. 24, 1860, pages 1301, 1302.

And here, just as in 1860, the principal component in the reserve is the comparatively *ap*preciated metal. The metals have indeed changed places; in 1860 the metal which had augmented in value was silver, now the metal which has increased in value is gold: but the position of the Bank of France is for the purpose now in hand identical. It now holds an enormous amount of gold, which it would be dangerous to pay away; just as in 1860 it held a much smaller though still considerable amount of silver, to pay away which would have been equally dangerous.

The basis of the difficulty is, that the French mint coins the two metals thus:—

One kilogramme weight of gold,	. . .	3,100 francs
" " " silver,	. .	200 "

or in the proportion of $15\frac{1}{2}$; but this is not the real proportion of the market value,—$15\frac{1}{2}$ is equivalent to about $60\frac{1}{4}d.$ for an ounce of silver, whereas the market price is now $54\frac{1}{4}d.$ The law having fixed an equation, bankers will always be in difficulty when the facts with which they must deal do not correspond to that equation.

Of course, as long as the Bank of France suspends specie payments it does not feel this difficulty; if we may be permitted to say so, it is on a lower level altogether. It is not perplexed by the possibility of having to pay in the appreciated metal, for it does not, except in minor sums and when it chooses, pay in any metal; but as soon as the Bank of France performs its legal obligations, the problem which the defective currency system of France sets before it must be solved. There is indeed one obvious mode of solving it. There is something very singular in a difficulty which is caused by holding a commodity which has enhanced in value: the obvious remedy is, to sell it in the market and to obtain the advantage of that value. If the Bank of France could sell its gold for silver at the present price, it would get a

large profit; it would have done a capital bullion transaction on a magnificent scale, and the shareholders would be large gainers in consequence. In 1860 the Emperor Napoleon, to whom the accounts of the Bank of France were then constantly submitted, would not permit this natural remedy to be tried; and therefore the Bank of France had to forego the profit, and to change away the dearer metal with the Bank of England. But now there can be no choice; the sums to be dealt with are so large that no such palliative by exchange can be thought of. If cash payments are to be resumed in France, large sales of gold for silver must precede and accompany the resumption.

And the effect of such sales will of course be to raise the price of silver as compared with gold. The circumstances of the Bank of France will make the possession of much silver constantly essential to it, and the effect of this new large demand will be a rise of price.

The only alternative is the demonetization of silver; and if this could be effected, it would give France a currency much better than the present one, according to our notions. The *bi*-metallic system is, we think, condemned by the very discussion in which we are engaged; for the perplexities which that system entails on the Bank of France are the evils of which we are seeking the remedy. But it may be doubted whether France is now prepared to abandon this system: it would be a very costly operation. The amount of five-franc pieces hoarded in France is probably very large; and if they are to be demonetized, gold must be substituted for them, — which, as the example of Germany shows us, is no easy thing to do. Moreover, till 1880, France is bound by a monetary convention with Italy, Switzerland, and Belgium, and can only change as they like. Even after 1880, France would not like to abandon the "Latin Union," as it is called, which is economically

convenient; which is her creation,—for it is an adoption of the money she desired,—and in which she takes a political pride. Probably, if silver is demonetized at all, it will be so at once, not only in France but in all those other states, which will be difficult to arrange and costly to effect. And it will not have the united support of theoretical opinion; for many Continental—and especially French—economists adhere to the two-metal plan. And even strong opponents of that plan (like ourselves) may well doubt whether this is the time to abandon it. The governments who do so, undertake in fact to substitute gold for silver; and just now they have unusual difficulty in getting the gold and in disposing of the silver. Germany is just making the substitution, and it is obviously an operation in which many great nations should not engage contemporaneously; an interval ought rather to be left after the completion of the operation by one before another begins.

It is true that the demonetization will be facilitated by the clauses in the agreement of the Latin Union which limit the number of silver pieces less than five-francs to be coined by each state in the union, and which limit the amount for which such subordinate pieces are legal tender. These pieces might therefore still be left to circulate as token money. But nevertheless the change, especially in so many states at once, would be a heavy task to accomplish, and not one which it would be easy to get undertaken; and failing this, there is no remedy except the sale of gold for silver by the Bank of France, of which we have spoken, so soon as a return to specie payments is determined on.

It may indeed be suggested that the Bank of France need not return to specie payments at all; but we do not believe that those who have managed her affairs so admirably during the last few years will even consider that alternative. As bankers who

have promised to pay on demand, they must wish to maintain their credit by so paying; and Paris can never again be the exchange center for Europe which it used to be, and which many concurring circumstances render it convenient for it to be, while bills on Paris are paid in a purely local medium like the paper of the Bank of France, and not in the precious metals, which are the money of all the world.

Sooner or later, therefore, we have no doubt that the Bank of France will resume specie payments; and then, unless the fundamental basis of the French currency law shall have been first changed, there will be a very material rise in the value of silver as compared with gold.

V.

THE EFFECT OF A DEPRECIATION OF SILVER ON OUR FOREIGN, AND ESPECIALLY ON OUR EASTERN TRADE.

[From the *Economist* of May 6, 1876.]

THAT the depreciation of silver as compared with gold, which has already begun, and of which we cannot yet predict the final amount, is unfavorable to the Indian government, is plain. That government receives a revenue in silver which it cannot easily augment, and it has to find annually, for the interest on its debt and for home expenses, a large sum of gold in London; whatever lessens the value of silver as compared with gold is therefore very disadvantageous to it, and whatever does so is also detrimental to the holders of Indian or other securities of which the interest is paid in silver. But it is only states or persons in this position — that is, those in receipt of a more or less fixed sum in silver — who will permanently be affected by it: after the depreciation of silver has attained its limit, trade will be exactly where it is now; and though during the

process there will be much unsatisfactory uncertainty in the trades with the countries whose prices are in silver, and though in some parts our trade will probably suffer, yet other parts will as probably be benefited. And therefore this change, though — like all changes in the value of a currency — a troublesome burthen, is nevertheless not an evil of the first magnitude, or at all likely to produce the disastrous effects — on English commerce especially — which we sometimes see expected from it.

We must remember that silver is still practically the main currency of a very large part of the world. The whole of the East uses it, not indeed to the entire exclusion of gold, but still much more than gold. It suits the minuteness of the payments which in Oriental countries, and in all countries in which there is no credit, of necessity make up almost the whole of the daily transactions which carry on common life, and for which the smallest gold coin that can be safely and economically used is very many times too great. Over the vast area of the backward pale of the world an incalculable quantity of silver is now scattered, doing the work of daily life, and doing it almost to the exclusion of all other currencies. And we must remember, too, that with this currency, as with all others, the efficiency depends on the value. The more things a rupee exchanges for, the fewer rupees will be necessary to do the work of India. A change of 10 per cent. in the purchasing power of silver would make 10 per cent. more silver necessary in each of these countries; and though we do not know what 10 per cent. would amount to, because we really cannot tell even approximately the quantity of silver circulating in those countries, yet we see that it must amount to something very large, for that present circulation must be reckoned by hundreds of millions. To make a permanent change even of small amount in the purchasing power of silver throughout the world is a most costly matter,

requiring much time. No [other] commodity is of so stable a value as a great deal of money diffused over many countries; because as soon as you diminish that value even a little, you augment the quantity required indefinitely. In this case, far more than in any other, an addition to the supply of itself generates an addition to the demand.

And a depreciation of such money is necessarily diffused with more or less rapidity through the various nations who use it; a local congestion, so to speak, is impossible. The laws which distribute the precious metals over the world will gradually lessen the value in all of them, if it is greatly and suddenly lowered in any one. There is a steady tendency to take such a commodity from the country where its purchasing power is small to those in which its purchasing power is great, and in that way this power settles in all countries at its level.

Such a change in the value of a metallic money will even generate a new trade between countries which had none before. The discovery of gold in Australia and California gave those countries a buying power which created a great direct commerce with them; the nations from whom they bought obtained a buying power too; so on with those from whom they bought: and so an unprecedented accession to the previous trade of the world [was created].

It would be absurd to expect any results of similar or approaching magnitude from the new silver mines in America, even were their magnitude and fertility many times greater than even the most sanguine computers make them; but the same cardinal principles will govern this smaller case which we have seen govern the greater. The silver prices of all articles must gradually and slowly be raised all through the silver countries; and the rise will be effected the most quickly in those countries which have most share in the commerce of the world, and which export and import most. Take the case

of India at this time. The depreciation of silver in London is an encouragement to English capitalists to buy commodities — jute, cotton, indigo, or whatever it may be — in India; such commodities are sold in rupees — that is, in silver — in the Calcutta market. Now, an English capitalist must first buy his rupees — for this is the real result of the more complex exchange transactions — before he can obtain these commodities; the cheaper, therefore, he can buy such rupees, the better his operation. Supposing an order to buy at a given hour in the Calcutta market to yield neither profit nor loss when rupees were at 2*s.*, it might yield a good profit if the rupee fell to 1*s.* 8*d.*, because then the gold of the English capitalist would go so much further in the purchase of them.

The very contrary arises in the case of English exports to India. The English exporter of these is paid in rupees at Calcutta or Bombay, and these rupees, when he brings them home to London, are worth say a sixth less than they used to be; and therefore he has a steady and certain motive not to export as much as he used to do. And the sure result of these two changes — of the encouragement of exports from India and of the discouragement of imports into India — is a flow of silver from hence thither, which must ultimately raise the general standard of prices there.

It may be objected that this rise of prices will be an evil to India, — will throw it out of the world's market; that Indian cotton, for example, which has thus risen in price, will not be able to compete with American cotton, of which the price will be unaltered. But this objection is fallacious: all which the rise of prices will effect will be, to withdraw the exceptional encouragement which, as we have just explained, the present state of things gives to the export of Indian cotton. When silver has settled to its new level of value, all trade, whether of export to or import from India, will go on as it did when it was at its old

value. Take the case of the English importer from India, silver having fallen say 15 per cent. in its relation to gold; he will get 15 per cent. more rupees than he used to do for his gold, but when he goes into the Calcutta market he will find that these rupees will only purchase an equal percentage less; his gold will be neither more nor less efficient than at first, and therefore he will neither be encouraged to buy nor discouraged from buying. Conversely, the English exporter to India will not be able to get as much for the rupees for which he sells his goods, when he brings those rupees home here; but on the other hand, he will have to a corresponding extent more rupees, and therefore the final outcome of his trade will not be altered.

No doubt it is true that during the process of depreciation, our general export trade to some countries will be under a disadvantage, — we shall export to them silver instead of goods; but on the other hand, certain other branches of our foreign trade will be augmented. The silver which we send to India we shall have sent to us from America, and we shall have to pay for it; and we shall doubtless pay for it in the same way that we pay America for the rest of the commodities which she sends us. Our present direct trade with America stands thus:—

	£
Export from America to England (1874), . . .	73,897,000
" England to America, " . . .	32,238,000
Balance in favor of America, ...	41,659,000

And against this balance America draws drafts to pay for what she buys in India, in China, or in France, and all over the world. The trade is what is called a "triangular" trade; because the debt due to one nation is paid for, not by the nation which owes it, but by some other nation or nations which are in debt to that nation. The more, therefore, we augment our American trade, the more we shall have to

export in goods; not indeed wholly, or probably principally, to America itself, but to other countries to which she is in debt. And as America always buys more in the East than she sells there, curiously enough one of the trades which will most likely be thus stimulated is the trade with the East, which from the first operation of the new cause — by the substitution of silver for goods in our direct trade — has been discouraged and depressed.

The same fact may be put in another way. The United States have acquired, by the extraordinary productiveness of their new mines of silver, an augmented purchasing power in the markets of the world; the increase of power they use in buying the commodities which they wish for in the East and throughout the world. But partly owing to her Protective system, and partly in consequence of natural causes, America has no direct communication with the countries which produce those goods; she therefore sends the silver to England, and England acts for her as a produce broker on a vast scale, — both sends on the silver to the countries which want it, and pays indirectly for what she buys to the countries she buys from. That we are able so to pay is one of the many instances in which, in trade, most is given to those who already have most: our export trade is so much greater and so much more easily augmented than that of any other country, because we are able to settle any debt in commodities far better than any other nation. If the United States buy of nation B, B is more likely to want something of England than of any one else; or if instead B buys of C, C is so likely: and so on through the alphabet, till at last you come to England. Our predominant international trade gives us, in a business such as this, an assured pre-eminence.

This is one compensation for any evil to our present export trade which may be caused by a change in the value of silver: and another is, that

a part of our import trade will, as we have seen, be benefited by the same cause; which must either cause — according to circumstances — increased profits to our traders or diminished prices to our consumers, and either way be a gain.

In thus writing, we have been content to assume that the American production of new silver will be on the largest scale which has ever been alleged, because we wanted to show how large the area of silver-using countries is; how slow, in consequence, will be the process of depreciation; how much of benefit as well as of loss there is to our trade while the process is going on; and how much commerce will return to its antecedent state when the change has run its course and the depreciation has terminated.

VI.

THE EXTREME FALL IN SILVER, AND THE HASTY REMEDIES PROPOSED.

[From the *Economist* of July 8, 1876.]

THE report of Mr. Goschen's Committee on the Depreciation of Silver has been laid on the table, and will doubtless appear immediately; and it is understood to contain a most full analysis of all the causes which have combined to produce this perplexing event. But in the mean time the fall of the rupee to 1*s.* 6½*d.* at the last bidding for Council bills, and of silver to 47*d.* per oz., have naturally caused the suggestion in various quarters of various hasty remedies; which can be discussed before we get the report, because by the terms of their reference the Committee were debarred from considering remedies, and told to confine themselves to causes.

The main evils of this depreciation are two. First, and most important, [one results from the fact] that the government of India receives the whole of its

revenue in silver, — partly in land rents fixed for considerable periods, and partly in taxes which it is difficult to increase, — and that this government has also of necessity to find in London a very large amount in gold annually; so that they lose a sum which, taking the rupee at 1*s.* 8*d.*, Sir William Muir, the Indian Finance Minister, estimated to be of most serious magnitude, and which, now that the rupee has fallen to 1*s.* 6½*d.*, will be considerably more. So grave a misfortune has seldom happened to any government so suddenly, and so completely from causes out of its control. Secondly, all private persons, such as the holders of rupee paper, who have to receive fixed sums in silver, lose, as is usual when a currency becomes depreciated; debtors gain and creditors lose, in this instance as in all similar ones. The great peculiarity of the case is the position of the Indian government, which has so great a burden so rapidly thrown upon it, and is so little able by additional taxation with equal rapidity to find means to bear it.

The remedies suggested are:—

First, that the government of India should demonetize silver and substitute gold; but those who make this proposal cannot have considered what in practice it would involve. A government which abolishes an old money must find a new one. It could not say, "Our law up to the present time has made the silver rupee legal tender; but we now change that, and make a gold coin legal tender, which gold coin you, our subjects, must find for yourselves." If the Indian government did so, the losses to its subjects would be enormous: every holder of the old coinage who wanted to pay a debt would have to sell silver, which is so rapidly going down, and buy gold, which in comparison is rapidly rising, and the loss would be severe. The only way in which such an operation can be effected is that which the German government has lately adopted. That government bought and found the gold which was to

form the new currency; and in so far as the operation is complete, has exchanged it for the old one. But no one could now propose this to the Indian government as a means of relieving itself from financial difficulty, for the cost which it would entail would be enormous. Even with all their resources, they would have great difficulty in getting the immense sum required in gold, and they would hardly be able to sell the silver at any price. The present position of the Indian Exchequer is not good, but it is beyond comparison better than it would be if this expedient were tried.

Secondly, it is suggested that we should adopt a double standard for India both of gold and silver; but this does not meet the difficulty. The effect of a double standard is, at every change in the relative value of the two metals, to fill the country with the metal which is falling. France in this way was during the cotton famine cleared of a large part of her silver, and gold was substituted for it; bullion dealers sent the gold to buy the silver, and made a profit of the transaction. The "bad money" always drives out the "good"; and the Indian Exchequer would gain nothing. The essence of the "double standard" is, to create two legal tenders and give the debtor the choice of paying in which he likes; the Indian ryot would of course pay in silver just as now, and the land revenue would be as much impaired, for the purposes for which it is wanted, by the depreciation of silver as it is at present.

Thirdly, it is suggested that the Indian government should cease to coin rupees; and that in consequence, though the value of uncoined silver fell, that of the coin would not fall, its supply being restricted. But the effect of such a measure would be, to reduce the price of silver far below even its present low amount; because it would stop the greatest natural demand for it, by stopping additions to the silver currency of India. And then, the difference in value between

the rupee as a coin and the same quantity of the uncoined silver would be much greater than it would be possible to maintain: good rupees would be a profitable article of manufacture, and would be imported largely from abroad and illicitly manufactured in India. Many governments have tried a similar expedient, and have in the end always been beaten and obliged to keep the price of their legal-tender coin near to the cost at which it can be produced; but in no case would the failure be so great as in that of India, because in none has the experiment ever been tried on a coin so important and of so vast a circulation as the rupee.

The effect also would be that the difficulty of disposing of silver in London, and the consequent lowness of the price, would become worse and worse. The natural cure for the depreciation of silver is, that it should be diffused over the globe, and especially over the immense area in the East and elsewhere which has a silver currency. If silver is depreciated 2 per cent. in all countries where it is the sole or main currency, 2 per cent. more silver must be required; and as the amount of silver in circulation in such countries is enormous, 2 per cent. upon it would be a very great demand, and take out of this market a very large quantity of silver. As we have shown on a former occasion,* the laws of trade will infallibly create this demand, though this action is necessarily slow. But the effect of not coining the rupee, in so far as it is successful, would be to suspend them altogether as far as India is concerned; because it is only by arresting the reduction in the exchange value of the rupee that this step can help the Indian government, and that reduction is the means by which, as we showed, the new course of trade is created, and the increased quantity of rupees required to do the work of Indian currency after that reduction constitutes the new demand for silver and the new use of it.

* July 8, 1876.

The example of the states called the "Latin Union" — that is, of France, Italy, Belgium, Switzerland, and Greece — is appealed to as a precedent for this policy, since they have limited their coinage of silver, as we have often explained. But their circumstances are very different from those of India. In France, which is so much the greatest, and also in Italy, inconvertible paper is really the ruling currency; it is that which settles prices, and everything has to conform to that. And even so the expedient is only regarded as a momentary one: it is acknowledged that the Latin Union must soon either return to the double standard and coin silver without limit, or must demonetize silver altogether. And if we did not coin rupees, the fall in the price of silver which it would cause would probably determine them to decide on its demonetization; whereas it is still possible that they may return to the double standard, which would raise the price of silver more than anything else.

This possible effect on the Latin Union is, however, but a minor reason for not thinking of this or any similar plan. The main reason is, that the fall in silver will be greatly lessened if we allow the ordinary action of trade to spread it through the world, so that the depreciation may be everywhere alike, and affect prices everywhere where silver is the currency; and that all plans which impede that action tend to keep the silver in this market, to enhance its depreciation here, and to prevent its diffusion which is the only cure.

VII.

THE REPORT OF THE COMMITTEE ON THE DEPRECIATION OF SILVER.

[From the *Economist* of July 15, 1876.]

THE Report of the Commons Committee on the Depreciation of Silver is a very able document. It

appears to have been drawn up by the chairman, Mr. Goschen, and accepted with comparatively minor amendments by the Committee; and it has the clearness, the precision, and the great information — no matter at what labor acquired — for which Mr. Goschen's writings on such subjects are remarkable. The Committee was excluded, by the terms of its appointment, from investigating remedies *eo nomine;* but by describing precisely the events which have happened, and analyzing as far as is possible the causes of each of those events, they have enormously facilitated the discussion of future policy. In all cases an accurate diagnosis of a disease must come before a discussion of remedies; and in a very complex case like this, such a preliminary is especially needful, or else we may find that we have been trying to cure disease A with medicine fit only for disease B, and so have made things no better, or worse.

The most striking cause of the depreciation of silver, and that which the Committee treat of first, is, the productiveness of the new mines in America; and looked at in this relation, the most remarkable thing about it is, its rapidity. In former analogous cases the effect has been much slower. Adam Smith was of opinion that prices in England did not even *begin* to be sensibly affected by the American mines till 1570, though the first shipments of specie were made in 1502, and though the mines of Potosi — the most productive of all — were discovered in 1542; and even then the depreciation was slight, and continued to increase only at a slow rate for many years. When gold was discovered in our own time so extensively in California and in Australia, most persons thought it would at once affect general prices; but it did not. Even yet there is a controversy on the subject; and though we believe that — especially since Mr. Jevons's investigations — there can be little doubt that a rise in gold prices has happened to some extent, we should

not like to state its extent precisely, and should fear to exaggerate it.

But now, the American mines were not much heard of in this country till last autumn, and the Committee tell us that the effect on the price of silver has been this:—

			d.		*d.*
1875	Yearly average, ...		$56\frac{7}{8}$		
1876	Fluctuations in January between .		$56\frac{1}{8}$	and	$54\frac{7}{8}$
"	"	February " . .	$54\frac{7}{8}$	"	53
"	"	March " . .	$54\frac{1}{8}$	"	$52\frac{1}{2}$
"	"	April " . .	54	"	$53\frac{1}{2}$
"	"	May " . .	54	"	52
"	"	June " . .	52	"	50

and as we write it is 48*d.*, showing a reduction of 16 per cent. from the average of 1875.

But we must observe that in this contrast we are not comparing the same things. This table is a comparison of the price of silver with that of gold only; when we spoke of the previous discoveries we spoke of the general prices of commodities. But there is no evidence whatever that general prices in any country where prices are measured in silver have risen in any such ratio; indeed, as we have understood, careful inquiry seems to show that they have not sensibly risen at all. General prices have obeyed in this case the same law as in former cases; they are being acted on very slowly. Indeed, it is evident that they must be so: if they had risen 20 per cent. over the whole of the countries using silver as their principal currency, or over any very large part of them, 20 per cent. more on the silver currency used would have been wanted to circulate commodities at those prices, which, as there are few "economizing expedients" in such countries, would have been a very large amount indeed. But no such new silver exists. The Committee say:—

"It is, however, an important and remarkable fact, to which it may be convenient to call attention at once, that though the increased production of silver in the United States is a fact beyond

question, no actual increase in the imports of silver from the United States to Great Britain has taken place since the year 1873, when the average price of silver was still 59¼*d.* per oz. Indeed, the amount of imports into Great Britain from the United States for the year 1875—viz., £3,092,000—is the smallest since the year 1869. In the same way, though the new currency laws of Germany affected a vast silver coinage, the sales of silver actually made up to the 26th of April in the present year do not appear to have exceeded £6,000,000, distributed over several years."

Except a small amount of silver which goes from San Francisco to China direct, all the silver which leaves America comes here; and therefore it is plain that no such additional silver as would be required by very greatly raised prices over the large areas of the East anywhere exists. General prices there have not risen in any such ratio as 20 per cent.; what has alone so varied is the relation of silver to gold in the London market, and in the markets guided by it.

But even this variation is most curious. Nothing like it happened when gold was discovered in Australia and California; it did not fall then in relation to silver at all as silver has now fallen in relation to it. The course of prices then was this:—

	Per oz.—*d.*
In 1848 the average price of silver was	59½
1849 " "	59¾
1850 " "	60 1/16
1851 " "	61
1852 " "	60½
1853 " "	61½
1854 " "	61½
1855 " "	61 5/16
1856 " "	61 5/16

which is certainly wonderfully little in comparison with what we now see, though the discoveries of gold then were every way as remarkable [as]—indeed, more remarkable than—those of silver now. The difference is certainly not from any excessively quick supply now. As the Committee shows, in 1875 the

silver sent from America was less than in previous years, and for the first six months of 1876 the figures have been these:—

IMPORT OF SILVER FROM UNITED STATES.

	£.
1874 (First six months), ...	2,046,925
1875 "	1,293,258
1876 "	1,293,851

so that in fact, notwithstanding the great fall of silver in this market, owing in great part to the apprehension caused by the new mines, we have had from them no extra supply as yet at all.

The explanation is, that the report of this new discovery came on a market where prices were previously falling, and which was most perturbed and sensitive. The Committee tell us that—

	d.	d.
Between 1862 and 1866 the yearly average price was between	62 and	61
Between 1867 and 1872 the yearly average price was between	61 and	60
In 1873 the yearly average was	$59\frac{1}{4}$	
" 1874 " "	$58\frac{5}{16}$	
" 1875 " "	$56\frac{1}{8}$	

showing a considerable fall. And they analyze the causes which were in action, weakening the temper of men's minds, and preparing them easily to allow of a still greater fall.

The first of these is the introduction of a gold currency into Germany in place of a silver one, of which the report gives a very clear and consecutive account. This cause, as our readers know, has been one peculiarly perturbing, because it has been incalculable as well as powerful. Dealers in silver have never for several years known either what quantity of it the German government was anxious to dispose of, or what price it would take for that quantity. Nothing depresses the tone of a market like uncertainty; and this subterranean political agency, if we may so describe it, has now for a considerable period been a cause of uncertainty, in incessant action, and

of the first magnitude. And its action still continues, — for the amount of the thaler silver currency which will have to be demonetized is most uncertain, the estimates of it differing by many millions; and therefore we do not in the least know either what the German government have in hand, or what they have to sell, or when they will have to sell it. The silver market is consequently affected exactly as the Liverpool cotton market would be if there was an immense unknown quantity to arrive. Such a market always, as the phrase is, lives from hand to mouth, sells as soon as it can, and the prices in it fall to an extent and with a rapidity which an observer acquainted only with the visible supply or the visible demand would not be able at all to account for.

The second cause is the policy of the Latin Union, to which we have so often drawn the attention of our readers. The states comprising it — France, Belgium, Italy, Switzerland (and now Greece) — in 1873 adhered strictly to the principle of the double standard of gold and silver; that is, they allowed any one to bring to the mint any quantity of either metal, and they coined it for him. In consequence, at every change they were always coining the metal of lesser value; and that metal, when coined, was used to buy and take away the metal of higher value. In this way, during the cotton famine France was half emptied of silver which was wanted for export to the East, and was filled with gold which was not so wanted. If these states had continued to adhere to this principle, the great effect on the general silver market produced by the German operations would have been much diminished and rendered scarcely observable. As soon as silver began to fall, it would have gone to France and been used there to buy gold, which had risen; thus silver would have been taken from the general market and gold would have been brought to it, till the former level of comparative values, or something like it, had been reached. But

France and the rest of the Latin Union could not endure this: partly from political and partly from economical motives, they would not take the "cast-off" German silver. They limited the amount of the silver which they would coin, and thus the silver market was at the same moment perturbed by two extra-commercial causes: one set of countries sold off silver as they had never before done, and so increased the supply; and another refused to take it in a way in which they had never before done, and thus diminished the demand.

Thirdly, there has been another cause, also not commercial, though of a very different kind, which has tended to diminish the demand for silver. This is, the increase in the amount which the Home government draws for upon India; as to which the Committee tell us:—

"The yearly amount payable by India for the disbursements of the Home government has risen since the Indian Mutiny from £5,000,000 to £15,000,000; a difference of which the magnitude will be appreciated when it is remembered that it is considerably more than half of the total amount of silver annually produced.

"That the full effect of this substitution has only been recently felt; as that effect was retarded by the construction of the Indian railways, which involved an expenditure in India of money raised in England, counterbalancing therefore an equal amount of expenditure in England of money raised in India.

"That the amount of the disbursements which has just been stated appears to represent the present normal expenditure of the Home government; and that therefore, unless by some marked change of policy, no diminution of that amount can be looked for."

The effect of this increase of the *tribute* (for such economically it is) which India pays to England is peculiar, because the ordinary relation of the two countries commercially has been peculiar. Generally the existence of such a tribute makes no difference in the amount of the precious metals transmitted from one country to the other. Mr. Mill explains this very clearly:—

"Commerce," he says, "being supposed to be in a state of equilibrium when the obligatory remittances begin, the first remittance is necessarily made in money; this lowers prices in the remitting country, and raises them in the receiving. The natural effect is, that more commodities are exported than before, and fewer imported; and that on the score of commerce alone, a balance of money will be constantly due from the receiving to the paying country. When the debt thus annually due to the tributary country becomes equal to the annual tribute or other regular payment due from it, no further transmission of money takes place; the equilibrium of exports and imports will no longer exist, but that of payments will: the exchange will be at par, the two debts will be set off against one another, and the tribute or remittance will be virtually paid in goods."*

But in the case of this increase of the tribute from India to England, the primary supposition of Mr. Mill does not hold. The exchanges were not before in what he calls "equilibrium,"—that is, one which did not admit of a transmission either way of the precious metals; there was a constant export of silver from England to India, a sum of money constantly paid by the dominant to the dependent country: and in such case the effect of an increase of the sum due from the dependency almost always at first is, and perhaps may permanently continue to be, a diminution of the cash which the superior country has to transmit. This is one effectual mode of rectifying the balance: it is the simplest, it is always the first taken; and it has been so here. From a most careful and valuable examination in the Committee's report, it appears that—

	£
Between 1868–9 and 1871–2, the annual average export of silver to India from England was	10,000,000
Ditto ditto 1872–3 and 1875–6, . .	4,100,000
Diminution, ...	5,900,000

But on the other hand, the increase in the "tribute money," as we call it, or the government drafts, is—

*"Political Economy," Book iii., chap. xxi., § 4.

	£
Between 1872–3 and 1875–6, the average of government bills on India was . .	12,600,000
Ditto ditto 1868–9, and 1871–2, .	7,400,000
Increase, ...	5,200,000

And the diminution in the demand for silver thus caused has been weighing on the silver market, making it constantly sensitive, and tending more and more to reduce the price.

These, with some minor ones on which we cannot dwell, are the causes why the silver discoveries now have produced so much more sudden an effect on the bullion market — that is, on the relative value of silver to gold — than the gold discoveries did on the relation of gold to silver five-and-twenty years ago; and surprising as that difference is, they are fully sufficient to account for it.

As to the discoveries themselves, the Committee speak with much caution. They very properly abstained from calling evidence from persons connected with the mines, as otherwise their report might have been made a "puffing machine," to raise the price of the shares in particular companies; they rely on the official documents which the American government issued, — the contents of which we have, we believe, laid before our readers from time to time.

They estimate the total yield of the United States: —

	£
Average annual yield from 1864 to 1867, .	2,300,000
Yield in 1872, ...	5,750,000
" 1874, ...	6,400,000
" 1875 (perhaps), ...	6,400,000
" 1876, "	9,000,000

These figures are not very large, and would come to very little when distributed over all the countries of the world which use silver as their standard of value; and in comparison with gold the effect is less, because the yield of gold from the new mines is itself very large. "Mr. Whitehill, the State Mineralogist" for the State of Nevada, the Committee tells

us, "states that 'During the past two years (1873 and 1874) this mine has yielded bullion to the value of $5,000,000, the principal of it since last June. The yield for September was $562,000, and for October $610,000. The daily yield of the ore is about 400 tons; about 44 per cent. of the value of the bullion is gold."

If in the end the supply of gold from these mines is increased on a sudden nearly equally with that of silver, the ultimate effects will not be at all like that which the recent state of prices has shown.

Now, from full information, we see the nature of the evil from which we are suffering. We are not suffering from a depreciation of silver as against commodities in the countries where silver is the standard [of] value; for there is no supply sufficient to produce such a depreciation, nor time if there had been such a supply to diffuse it, and there is no such depreciation in fact. We are not suffering from a depreciation of silver as against gold caused by a sudden excess in the supply of silver; for the new supplies of silver have been only moderate, and none of them have come here. We are not suffering from a depreciation of silver as against gold caused by a diminution in the cost of production of silver; for there has been no time, or anything approaching to time, to say what the ultimate cost of production will be. No doubt certain mines of singular fertility have been discovered: but it is not silver produced in the best mine which determines the price of silver as a whole, any more than it is the corn grown on the best land which determines the price of corn as a whole; that which does determine it is, the cost of production in the worst mine which can maintain itself in working. The producer in the least favorable circumstances always fixes the price; those in better circumstances take that price, and get an extra profit. And what that mine will be in the case of silver we cannot as yet tell; the experience of years

alone can determine it. All that we can now safely say is, that judging from all past similar events it will not be any of the new mines now discovered, or any of fertility approaching to theirs, but some other far down in the scale; some one which has been in some degree better than some others till now, and therefore will be able to maintain itself when those others are obliged to desist from working.

What we are suffering from is, the apprehension of increased production of silver suddenly supervening on a market previously perturbed, upon which one government had forced an extra supply, from which a union of other governments had refused to take as usual any supply, and in which another government, by an increase of the tribute it requires from a silver-importing country, has temporarily if not permanently lessened the demand.

This explanation of the real malady at once disposes of a crowd of unreal remedies. No competent person can propose a demonetization of silver in India, and a substitution of gold for it, just at a moment when the price of silver has been thrust down by so strong an apprehension caused by such peculiar circumstances. It would be to require the Indian government to buy the largest amount of gold ever bought in the dearest market for gold, and to dispose of the largest amount of silver in the cheapest market for silver, which ever existed. The present financial position of the Indian government is no doubt impaired by this sudden depreciation of the metal in which it receives its revenue: but the remedy for a minor deficit would bring in, in lieu of it, a deficit of the first magnitude; it would be nothing else but financial ruin.

Again, no one would propose to arrest coining silver in the East as a remedy for such a state of things; for this would only disorder the silver market still further. It would add a new political difficulty to those previous political difficulties which have

caused so much disturbance, and so make the existing confusion far worse than before.

Nor can it be maintained that the Indian government should now require the ryot, whose rent has been formerly fixed in silver, to pay either in gold itself, or in so much more silver as would purchase the same quantity of gold as that fixed rent would have purchased when the settlement was made. If silver in India had become depreciated as against commodities in general, it might have been possible to say to the ryot, "You are selling your commodities for more silver, and therefore it is not unfair to ask you to pay us — the government — a proportionate amount more." Even then the ryot would have been probably discontented; he would have said, "If prices had gone down the government would never have let me off, and it is not fair that they should take the benefit of good times when they leave me the misfortune of hard times." Still, in this case, if the depreciation of silver had been against commodities in general, it would have been perhaps substantially, though not intelligibly, equitable to adopt such a policy; but now that there is no such depreciation of silver as compared with commodities, such a scheme is not feasible. The ryot in India does not sell his produce a bit dearer than he did a year ago; his income, as yet, is just what it was, and it must be so till a vast amount of silver has gone to India to raise the prices of daily life. Clearly, therefore, he must not be additionally taxed because the silver market is apprehensive, and because certain governments (the Indian government being one of them) have perturbed it.

The real remedy, as we have shown several times, is, to leave the great natural forces of trade to operate unrestricted. The true remedy for an enfeebled market is an access of demand; and in this case the laws of commerce, if not suspended or crippled by state interference, will produce that demand. The necessary effect of a depreciation of silver as against

gold is, to give a bounty on exports from India and the other silver-using countries to England. An English merchant can now buy many more rupees than he formerly could with the same number of sovereigns, and therefore he can import from India, though prices at Calcutta are not at a level at which it would have paid him to operate if he had not had that novel facility in getting rupees; similarly, shippers to India cannot afford to sell at the same price in rupees which they could have formerly, for they will lose in bringing those rupees home: and the combined effect of this bounty on exports from India and of this fine on imports into India must sooner or later be an unfavorable balance of trade, and a consequent flow of silver to the East. A new demand of great magnitude will eventually relieve the silver market, if we only leave it alone.

It has been objected that as yet this process has not begun. But in this complexly organized world, it is never safe to reason that a force, even of great magnitude, does not exist because its effect may be impeded. No doubt, as the first table we print at the end of this article shows, the exports from India to this country have in many instances not increased, though in some they have; but then table No. 2 shows why, — the prices of those articles in England have gone down, and therefore, though there might be a gain in comparison with last year on the exchange, there might be a loss as compared with last year on the whole transaction. As to the diminution of profitableness of shipments *to* India from hence, there is unhappily no doubt. Every trade circular dealing with the East records — every Chamber of Commerce in cities interested in the East resounds with complaints — that it is so. Sooner or later this must cause a large diminution in that branch; a diminution, no doubt, universally to be much regretted, but nevertheless an evil necessary to be endured, because it is part of the appropriate remedy at the present time. We have spoken of India

because that is the silver-using country which comes most easily to an Englishman's mouth; but the same thing is true of China, of the whole East, and of every other part of the world. To them all, there must ere long be an export of silver. In a time when the speculative part of the business world were eager and animated, this would have happened long ere this; but even the present indisposition to begin new things, and the recent ruin of so many of those who were most disposed to do so, cannot long delay it.

At what price silver will settle down, nothing but experience can determine: but the two cardinal points in the matter are, first, that that price will be determined by the cost in the *least* good mine which pays to keep at work; secondly, that the extra demand for silver to countries where it is the standard money will require a very large sum, if the value of silver as against commodities is to be depreciated in all of them, because the efficiency of a metal as money depends on it,—by whatever percentage you depreciate it, you make it necessary by that very percentage, *cæteris paribus*, to have more of it. And as the quantity of silver now circulating is immense, even a small percentage on it comes to a good sum; so that ultimately mines of far inferior grade to those now so much talked of will continue to be worked, will settle the value of silver, regulate its price, and in all likelihood prevent any such depreciation of it as the peculiar perturbations of the present moment have led many to apprehend.

TABLE OF PRINCIPAL ARTICLES IMPORTED INTO THE UNITED KINGDOM FROM BRITISH INDIA.

		First Half-Year.			
		1876.	1875.	Increase.	Decrease.
Wheat,	cwts.,	1,166,000	119,000	1,047,000	
Cotton,	"	1,152,000	1,617,000		465,000
Hemp,	"	29,000	57,000		28,000
Hides, dry,	"	187,000	218,000		31,000
Seed, flax and linseed,	"	603,000	205,000	398,000	
Silk, raw,	lbs.	89,000	244,000		155,000
Sugar, unrefined,	cwts.,	47,000	205,000		158,000
Tea,	lbs.,	9,903,000	10,708,000		805,000
Wool, sheep, and lambs,	"	13,117,000	10,194,000	2,923,000	

AVERAGE PRICES OF IMPORTS FROM BRITISH INDIA.

First Half-Year.

	1876.	1875.	Increase.	Decrease.
	£ s. d.	£ s. d.	s. d.	s. d.
Wheat, . . . per cwt.	0 10 0	0 9 5	0 7	
Cotton, . . . "	2 9 6	2 15 0		5 9
Hemp, . . . "	0 19 5	1 1 9		2 4
Hides, dry, . "	3 15 0	3 19 9		4 9
Seed, flax and linseed, per qr.	2 9 3	2 14 3		5 0
Tea, ... per lb.	0 1 8⅜	0 1 9⅛		0 0¾
Wool, ... "	0 0 9¾	0 0 10¼		0 0½

VIII.

THE PROPOSAL OF THE BENGAL CHAMBER OF COMMERCE TO SUSPEND THE COINAGE OF SILVER IN INDIA.

[From the *Economist* of Aug. 5, 1876.]

THE Chamber of Commerce of Bengal have resolved "that it is expedient for the government to suspend clause 19 of Act 23 of 1870, which makes it obligatory on the Indian Mint to receive all silver tendered for coinage;" as also "section 1 of clause 11 of Act 3 of 1871, which makes it obligatory on the Currency Department to issue notes against silver bullion sent in, and that during such suspension it be unlawful to import coined rupees." The weight of the authority of that Chamber has therefore been given to the proposal to suspend the coinage of silver, and thus to maintain the value of the rupee by diminishing the numbers of it in circulation, although the silver out of which it is made is falling in value.

The effect of this plan would be, as is obvious, to hold out the greatest stimulus to private coinage which has ever been given in the world. The basis of the whole proceeding is, that the silver as a metal is likely to fall much and rapidly in value, in consequence of the new mines in America; but if this is so, the Americans will not lose the Indian market if they can help it,— if the government will not coin these rupees they will do it for themselves, and

no law will be able to keep what they coin out of India.

We have also proved that this plan would have the necessary effect of suspending the natural cure for the present evil. The silver market is now disorganized, not by a great supply but by an excessive apprehension; and the proper cure for such a market (and it is often a rapid one) is a brisk demand. Now, the nature of the present fall in the exchange value of the rupee is, as has been at length explained, to give a bounty on exports from India, to give a discouragement to imports into India, and thus to create a balance of trade favorable to India, and a flow of silver thither. As there is no excess of supply in the silver market, the demand thus created will greatly sustain its value.

But there are other objections than these to the plan, which, as they arise from its bad effect on Indian trade, should have prevented the Bengal Chamber of Commerce from recommending it. A metallic currency of which the quantity is artificially regulated, of which whoever likes cannot get as much coined as he wishes, is as much a currency of fictitious value as a currency of inconvertible paper; and a nation which takes it is exposed to the same evil. A rupee "limited"—that is to say, a rupee of which the numbers could not by law be augmented—would do in India much what the greenback has done in America; it would be an appreciated artificial currency instead of a depreciated artificial one, but it would be an obstacle to commerce, and would tend to isolate the country exactly in the same way.

In dealing with America now, as we need not explain, there are two problems for the English exporter: he has to consider for how many greenbacks he can sell his article, and then how much "sterling exchange" he can buy with those greenbacks. In dealing with a country which has a metallic currency, there is always a limit to the fluctuations of

exchange; the premium on bills can never rise beyond "the specie point,"—the point at which it will pay to export gold or silver, as the case may be: but in the case of a fictitious currency there is no such final point, for that currency cannot be exported,—the premium on bills may rise to any height, as the depreciated paper is more and more multiplied. Upon an average, any extra-high paper price for his article obtained in America by the English merchant will be compensated by an equal loss on turning the paper into sterling; when other things rise in paper price, the paper price of gold as a rule will rise too, and with it the price of bills on London payable in gold. But though this is the general tendency, and a perfectly sure tendency on the average, it is only so sure on the average; it may fail in a particular case, and very often does. During the Civil War, and at other times when gold has been an article of great speculation, the fluctuations in the premium on it have been very violent; and there were no corresponding fluctuations in commodities, because there was no similar speculation in them. At other times there might be speculation in commodities not shared by gold or bills. And thus the whole trade is confused: the profit is uncertain, because it depends in the long run on the counterbalancing effect of two bargains, and very often the two do not counterbalance.

All persons engaged in the American trade are most anxious to get rid of this impediment: but the effect of the scheme of the Bengal Chamber would be to introduce into the Indian trade a similar impediment,—only, so to speak, with the other side turned up; prices in India would fall, not rise, in consequence of the non-coinage of the rupee. We must remember that the currency of a stationary country requires constant renewal, and that of a progressive country requires constant increase; and therefore, if you keep the quantity fixed, prices are sure to fall.

And as the rupee cannot be imported, there is no check on this fall. Smuggling rupees apart, the decline will continue so long as the fixity in quantity of the rupee is maintained, and it will be quicker or slower in proportion as the increase of the country is so.

No doubt the price of bills on England will in the long run fall too, like that of other things: there will be less money as a rule coming to England, because English imports into India have sold for less; but there will be no reliance on this being so in any particular case,—the trade will be in confusion. As long as silver can pass as money between the two countries, there is a limit to fluctuation in exchange; but the moment you limit the coinage of the rupee, you prevent that passage. Silver, if the Bengal Chamber have their way, will be quoted with incessant fluctuations in Calcutta, just as gold is in New York; and its price and that of bills payable in it will be as much liable to the influence of speculation.

Though on the whole this appreciation of the coin rupee would probably be better than the depreciation of the greenback, its first effects would be more painful. The fall in prices would make people think that they were getting poorer; whereas in the opposite case, the rise makes them imagine they are getting richer. And the "contraction," as Americans call it, would raise the rate of interest: there would be less money to lend, just as in the case of depreciation there is more money to lend,—again a painful effect instead of a pleasant. Both are temporary; the change of prices makes the desire of persons to borrow less in the one case or more in the other, and that change likewise makes their power of borrowing less or greater, because the value of securities decreases or increases. Still, for the time, the first effect of an appreciation is not pleasant; and neither the Indian nor any other mercantile community which has been exposed to it has ever liked it.

And then, what is to be the end? Either the depreciation of silver depends on passing causes, and then this appreciation is needless,—it would be better not to disturb the ordinary course of trade: or on the other hand, the depreciation of silver is more or less to be permanent, and then this appreciation of the rupee is mischievous; it will cause a motion of prices in the wrong direction to the natural one; it will cause prices to fall just when, from the legitimate effect of circumstances, they should rise. And this wrong movement will have to be corrected, this artificial rise will have to be undone; and so, in addition to the inevitable fall of the value of the rupee *with* that of silver, there will be a needless fall of the rupee *to* that of silver.

An idea seems indistinctly to float in many minds that in this way an opportunity will be obtained for introducing gold. But how will it be gained? The difficulty of introducing gold in place of silver is, that you must demonetize silver and give gold in place of it; but the silver is so great in amount that the Indian government could hardly get gold to replace it, and could never afford the cost of the change. No doubt there would be fewer rupees in circulation the longer the coinage was suspended; but then each of these rupees would be of higher value as coin than as silver, and when it came after the demonetization to be sold as silver, there would be so much extra loss.

It is asked, too, Why should not we do in India as the Latin Union do in Europe; why should we not assume their "expectant attitude"? But the cases are not similar. In India, silver is practically the only legal tender; in France and Italy it is one of three, and in the rest of the Latin Union one of two. The main currency in the first two countries, which are by far the greater and richer part of the Latin Union, is inconvertible paper, which is now really the standard, and not metal at all; and in the other

countries gold circulates as well as silver: so that practically, silver is only a subordinate currency in the Latin Union, taking it as a whole, and therefore the limitation of its quantity does not cause prices to fall, for prices are not measured in it. The scale is so much smaller, too, that false coining has not yet operated, any more than it does in our own token coinage. And the whole position is different. The Latin Union was a group of double-standard countries largely using gold; and the question for them is, whether they will give up their gold and become silver countries exclusively,—which would happen if they were to abandon the limitation of coinage while silver is as cheap as now,—or whether they will demonetize silver and use gold as a standard only. This would be troublesome and costly, but still it could be done. But India has no problem to consider: she is irrevocably committed to a sole silver currency; and therefore a similar attitude would in her case, besides being mischievous, have no meaning.

The true remedy, as we have often shown, is not to impede silver's going to India, but to permit the laws of trade to diffuse silver through India and through the world. This will cause an immense demand for silver, for the countries where it is the only currency are still vast and numerous.

IX.

THE DEBATE ON THE INDIAN BUDGET.

[From the *Economist* of Aug. 12, 1876.]

THE whole interest of the debate on the Indian Budget centered in the discussion on the value of silver. Independently of this, the finances of India were in a fairly good position; as compared with that of most governments in the world, a very good one. It is true that if you include the amount

expended on reproductive works, there is a deficit of about two millions last year, and that there always is a large one; but then, few other governments make any similar expenditure and treat it in the Budget as the Indian government does. And for many purposes this way of spending money must be separated from others: it is at least *meant* to be an investment, which no other kind of government expenditure is; and you have to discuss in relation to it, commercial questions of profit and loss, with which in the accounts of governments you have ordinarily nothing to do. With these we need not now meddle; those who at this moment care most for the matter care for it in relation to the depreciation of silver, and to nothing else.

Lord George Hamilton estimated the loss by exchange at £2,312,000 for the year 1876–7, but he did not expect a deficit as against the *ordinary* expenditure in consequence. On the contrary, he reckoned—

	£
Revenue, ...	50,480,000
Ordinary expenditure, ...	50,336,000
Surplus, ...	144,000

a result which he said was very good, and which no doubt is so if (which we do not now deny) the extraordinary expenditure is good and proper.

This loss on exchange arises, as the report of Mr. Goschen's Committee showed, in two ways; first, from the depreciation of silver; and next, from the increase of the Council drafts,—of what may be called the "tribute" from India. As to the first, Lord George explained very clearly that the Government had no intention of touching now any of the remedies which have been proposed,—either the suspension of silver coinage, or the introduction of a gold one, or an adjustment of the land revenue. And he assigned what seem to us to be excellent reasons for so doing; which we need not, however, give at length, as we have at various times placed them before our

readers. He said, too,—what is well known, but what it is nevertheless desirable to have confirmed by official authority,—that the natural remedies were operating; that the price of Indian commodities measured in silver had not risen, and that in consequence a great encouragement had been given to the exports from India, which would cause a demand for silver here, and would relieve the market. And we may now expect that this process will go on more rapidly than before: one great cause of hesitation has been the fear that Government might "do something,"—something that might be anything, and which would derange the usual course of business; but now that the wise policy of the Government has been announced, there will no longer be any such fear of disturbance.

Mr. Goschen added on this point the weight of his authority—especially great, as having recently elaborately investigated the whole subject as chairman of the late Committee—to that of the Government. He showed at length that none of the plans which had been proposed were at present at all fit for adoption; and he said especially that he had seen statistics which seemed to show that prices had not risen in India, which all other information confirms. And even without statistics, common-sense would show that such is likely to have been the case: a great rise in the price of all commodities through a country using a metallic currency only requires a great increase in that currency to carry it on. But no such amounts of silver have gone to India, or anything like them, as the following figures show:—

IMPORTS OF SILVER INTO INDIA.

Net Imports (after deducting Exports).

	£
In 1866–67,	6,960,000
1867–68,	5,590,000
1868–69,	8,600,900

In 1869–70,	7,320,000
1870–71,	940,000
1871–72,	6,515,000
1872–73,	705,000
1873–74,	2,450,000
1874–75,	4,640,000
And in the year just concluded, *i. e.*, 1875–76,	1,555,000

And therefore silver prices cannot have risen, for there has been no silver to raise with them. The indisposition to admit this arises from not understanding the distinction between the depreciation of silver, which we elsewhere explain,* as against gold in a market where it is not a money, and its depreciation as against commodities in a market where it *is* a money; when this distinction is clearly seen, there is no longer any difficulty in this part of the subject.

As to the second element in the loss by exchange, — the "tribute," as it may be called, — the Government stand in a very different position. They are bound to do something here, for they have to bring home their money from India; but they are not bound to bring it home except in the way in which they lose the least, — or rather, they *are* bound to bring it home in that way. There could be no objection at times to their lending money in India and borrowing it at home at the same moment, if the time did not appear favorable for bringing it home; and they can choose any mode of remittance they think best, — it is merely a matter of business, like the remittance of any other money: and this Lord George Hamilton very well explained. Of course, however, the finance policy of the Government should be calculable, and the amounts for which it is going to draw on India should be made known some time in advance; as otherwise they will make business uncertain, and so diminish it.

* See Chap. x.

X.

THE DIFFERENT EFFECT ON TRADE OF A CHEAPENING OF THE PRECIOUS METALS, AND OF A DEPRECIATION OF INCONVERTIBLE PAPER.

[From the *Economist* of Aug. 12, 1876.]

We showed last week that neither the depreciation of an inconvertible paper nor the appreciation of an artificially limited coin produces as a rule any effect on trade. What an English exporter to America gains on the one hand, in the additional price for his goods consequent on the depreciation of greenbacks, he loses on the other by the additional price which he has to pay for gold, or a bill payable in gold, which he requires to bring that price to England. Greenbacks are of no use here, and their depreciation upon an average, though by no means always in every particular case, affects the prices equally of all things; it is a local depreciation, beginning in a particular country, affecting alike all the property and products of that country, but affecting nothing out of it.

But it is necessary to distinguish this most carefully from a depreciation of the precious metals caused by a large new supply. That new supply is a new exportable product, sent from the country of its origin through the world, and thus affects more or less, in proportion to its magnitude, the world's trade.

Suppose, for simplicity, that silver were the *only* precious metal in the world, — that all nations used it as money, and that none of them used gold in that way at all: the process of depreciation by such new supplies as are expected from Nevada would be this: —Prices in Nevada and in the rest of the United States would rise; in consequence, imports into the United States would tend to increase, exports from them would tend to decrease: and so, an unfavorable "balance of trade," as the phrase is, being created, silver would be exported; it would be the best way

in which America could pay for her imports, and she would so pay for them. On the other hand, the country from which those imports came — suppose it was India — would receive that silver; and in proportion as it received more and more, its prices would be more and more raised. What happened in consequence of the new silver in the country of its origin, will again happen in the country of its first receipt: imports into that country will be stimulated, exports from it checked, an unfavorable balance of trade created, and silver will be sent to the countries which it has to pay. Then in their turn these countries — the countries of second receipt, as we may call them — will undergo all the same changes. The depreciation of a depreciated paper is a stationary depreciation, fixed in the country which makes the paper; but that of a precious metal is a *traveling* depreciation, which passes slowly over the civilized world, altering trade everywhere, creating a new article of export first from one country and then another, and in consequence generating a new trade of export to pay for it in the country which receives it.

The *modus operandi* of this process is much affected in the usual state of the world by there being two precious metals used as money, — gold and silver, — and also by gold being in many ways the principal of the two; but though the detail is changed, the principle is the same. In a country which uses gold only as a standard currency, silver is a commodity having its price only in gold, just as silk or cotton; that price goes up and down in the same way, and is quoted in the same way. And London is the principal center of the wholesale commerce, and especially of the new wholesale commerce, of the world. We buy more readily than any other nation, for we have much more money than any other of equal enterprise; and therefore all great business requiring new capital on a sudden comes here. Accordingly, the new silver for the most part goes not straight to

India and the East, where it is a money, but to England, where it is a common article; and we send it over the world and to the nations where it is a money. But this is only a change in the *route* of the depreciation; it interposes a sort of house of call, it does not change the essence of the matter.

No doubt the first effect has been, to advertise and make far more obvious than it would otherwise have been the depreciation of silver. If silver had been our money, as gold is, we should scarcely have been as yet conscious of its being depreciated. A few millions more silver (from Germany or elsewhere) would have gone into the Bank, would have eased the money market, and have tended to raise prices; and we should have had to pay for that silver, just as we pay for the gold which *does* come; but this process would have been very gradual, — probably as yet nearly unfelt. The ready demand for silver as a currency in England would have much maintained its value here. You could not have depreciated it much without increasing its quantity — both the quantity in the Bank and the quantity in out-of-door circulation — very largely; but as silver is not a money except as a token, — not a money regulating prices, not a money [of] which more and more is wanted as the value falls more and more, — there has been no new English demand of equal or comparable size. Some more silver may, in consequence of the cheapness, have been taken for the arts, but this is all. The actual supply from Germany and the apprehended supply from America have come to a market which other circumstances had made bare of demand; they generated no new demand, and in consequence there is a great fall in the value of silver in England. The traveling depreciation has come here and has been intensified, as has been shown.

This sudden fall in the value of silver in England has caused a corresponding alteration in the exchange with the countries whose money is silver. As is well

known, between two countries which use the same metal for money, there is a natural and fixed par of exchange: a certain weight of that metal of a certain fineness, in the currency of one of these countries, will always exchange for an equal weight of like quality in the currency of the other. But between two countries one [of] which employs gold and the other silver, there is no such natural par, — the relation between the two currencies depends on the amount of the one metal which will exchange for a given amount of the other. When, as now, that amount much varies in England, there is an immediate change in the relation of the English gold currency to foreign silver currencies; because the amount of gold which it would take here to buy any given amount of silver, to export it and coin it into those silver currencies, varies.

And this is the process by which the depreciation travels on another step. Silver being cheaper here, more of it will be bought and sent to the countries where silver is money; but its value there against commodities will not fall as suddenly as it has here. We see that it would not, if silver had been the only metal used as money in the world; and the countries where it is used are, within their own boundaries, in the same position. The more silver falls in purchasing power, the more of it will be wanted to purchase commodities; and the demand for it, therefore, will increase incessantly where the supply is augmented. The silver prices of commodities will be slowly raised everywhere where silver is money, and a great deal of it will be required in the process, and the course of trade will be changed: the silver countries must find exports to pay for this new article, silver, which is coming in upon them.

We must therefore carefully distinguish two things which are often confounded in discussing this subject.

First, we must see that a depreciation of a metal used as money, whether silver or gold, is utterly different in its effects from those of a depreciation of

a currency of paper; for it creates an international trade, and that of paper a local one only.

Secondly, we must see that the depreciation of silver in London, where it is only a commodity, is a wholly different thing from its depreciation in countries where it is a money. The first, as we have seen, is very rapid, but the second is very slow indeed; and the second will counteract the effect of the first, as it is now daily doing, and will tend to raise the value of silver in London — in the *entrepôt* where the market is so sensitive, — by distributing it over vast regions where much more will be wanted if the value falls comparatively but a little.

Thirdly, we must observe that this process is not at all bad for the trade of England. No doubt the fall in the rate of exchange is a disadvantage to shippers to the countries where* money is silver; but then another class of exporters will be benefited, for we import that silver and have to pay for it. The loss on the other† hand will be counterbalanced by a gain on the other.

XI.

THE AMERICAN COMMISSION ON THE CURRENCY.

[From the *Economist* of Sept. 21, 1876.]

THE last act of the Congress was to appoint a commission to consider and report on the currency question in its various present bearings; that is:—

"First, into the change which has taken place in the relative value of gold and silver; the causes thereof, whether permanent or otherwise; the effects thereof upon trade, commerce, finance, and productive interests of the country, and upon the standard of value in this and foreign countries;

"Second, into the policy of the restoration of the double standard in this country, and if restored, what the legal relation between the two coins, silver and gold, should be;

*† Obvious misprints for "whose" and "one." — ED.

"Third, into the policy of continuing legal-tender notes concurrently with the metallic standards, and the effects thereof upon the labor, industries, and wealth of the country; and

"Fourth, into the best means of providing for facilitating the resumption of specie payments."

And this commission will no doubt be of use to European economists in collecting information as to many American matters connected with the currency, upon which it is now very difficult to find a trustworthy authority. But as far as respects the practical questions to be determined in the United States, "half would have been more than the whole;" it would — at least if we may judge at this distance — have been much better to restrict the commission to fewer points, than to empower them, as has been practically done, to inquire into anything and everything as to American currency. In the heat of a presidential contest, the commission must be active-minded indeed if they can thoroughly work out all this.

The set of facts most wanting inquiry certainly is the new set, — that relating to the change in the value of silver. The conditions of resumption, the mode in which a satisfactory paper currency should be maintained after resumption, are old matters, on which American statesmen can find no difficulty in obtaining information quite as good as this commission will collect for them. But the present relative position of silver and gold is a perfectly new thing in the world; and America, as a principal producer of both, and as having to settle whether she will have a currency of both or either, ought certainly to investigate it as soon and as completely as possible.

The cardinal present novelty is, that silver and gold are, in relation to one another, simply ordinary commodities. Until now they have not been so: a very great part of the world adhered to the bimetallic system, which made both gold and silver legal

tenders, and which established a fixed relation between them. In consequence, whenever the value of the two metals altered, these countries acted as equalizing machines: they took the metal which fell, they sold the metal which rose; and thus the relative value of the two was kept at its old point. But now this curious mechanism is broken up; there is no great country now really acting on this system. The "Latin Union," it is true, adhere to the name, but they have abandoned the thing: as they do not allow silver to be coined except in limited quantities, they have no longer an equalizing action; they no longer receive the depreciated or part with the appreciated metal, and therefore the two metals now exchange for one another, just as other commodities.

The gold price of silver is now like the gold price of tin, — left practically, for the first time in history, without artificial regulation, and free from the manipulation of governments; and it is into the consequences of this that the United States should now inquire, for they have nowhere been fully treated of.

The first effect is that to which M. Léon Say drew attention not long ago, in a speech of much ability, — the *instability* of the value of the two metals. In former times, he justly said,* the fluctuations in the relative value of the two metals were few and small, but now they are many and large. Particular causes, no doubt, aggravate that instability at this moment, — especially the demonetization of silver by Germany, and the supposed likelihood of great supplies from Nevada; but though the instability is aggravated by these causes, it is not created by them, and it will not cease with them. There is no inherent reason why the gold price of silver should be uniform, any more than why the gold price of platinum should be the same. The old notion of extreme steadiness is one generated by the practice of governments, and which has ceased when the practice ceased and will not revive till it revives.

* I have canceled the perverting word "that" here. — Ed.

The United States, therefore, which have a "money" to choose, must observe that they have three courses to choose from, and must see what are the consequences of each.

First, they may choose the old bimetallic or double-standard plan; but if they do, they must make up their mind to be always changing their coinage. The natural value of the two metals now being, as we see, fluctuating, a nation which takes both will be incessantly changing from one to the other; it will always be taking the worse and giving the better. The existence of such a country or set of countries is an advantage to the world at large, — because, as we have seen, it preserves a uniformity between the two metals, one or other of which is used by all civilized nations to count value; but the expense and inconvenience of a changing currency are great, and how far a nation would be wise to undergo them for the good of the world, we are not sure. She herself obtains no advantage: she sells gold for silver or silver for gold, and the brokers get their commission; but this is all. And to a great borrowing nation like America, it would always be an objection that she would pay in the worse coin at the time of payment, whatever it might be. At the present moment America would become a silver country, and the interest and principal on her obligations would be paid in silver. The evil, of course, would not be what the momentary circumstances of the market would now suggest: silver would not be at 52*d.* per ounce if America was a country with a sole silver currency; so large a demand as her coin requirements would send the price up very rapidly, — perhaps to its old amount. Still, as the debts of America are so large, the probable objection which a lender might make to the certainty of his having to accept the inferior mode of repayment is to her important; she would possibly have to borrow on terms somewhat less good.

Secondly, the United States might take the single gold standard like ourselves; and this is what, till

very lately, every English economist would have advised them to do, — the evils of this plan had not then been seen, but its good was very apparent. That all great commercial nations should have the same metal for money is, *per se*, a plain gain. The objection is, that there may be some difficulty in getting the gold for so many, very rapidly. The total production of gold, according to the estimate laid before the Silver Committee, for recent years is —

	£
In 1872,	17,569,000
1873,	21,946,000
1874,	19,880,000
1875,	20,353,000
Total,	79,748,000

or nearly £20,000,000 a year. And this is not at all a large amount to provide for the yearly uses of the world.

In the 18 years from 1858–75 the imports of gold	£
into the United Kingdom were	331,179,000
Exports from	251,413,000
Total absorption in 18 years,	79,766,000

or at the rate of £4,432,000 a year, being more than one-fifth of the whole. So that if Germany, America, and perhaps the Latin Union, were all to take to a gold currency, there would certainly not be too much gold; probably the money markets of the world would be straitened by there not being sufficient.

The third and last course open to the United States is, to make silver their sole standard. A few weeks ago this would have been generally deemed to be beyond the limits of consideration; at that time there was a panic, and it was imagined that the price of silver was going to fall lower and lower till it became worth hardly anything. But experience has now shown, as theory always suggested, that

there would be a demand for silver for the East consequent on its cheapness; that this demand would grow with its cheapness: and then an almost indefinite quantity, if supplied, would in time be taken off the market. As the supply here is small, the price has risen rapidly, though it has for a moment been checked again by the financial operations of the Council of India in drawing for their tribute. The extreme panic as to the price of silver has therefore passed away, and we are able to consider calmly whether it would be wise for the United States to take it for a standard of value or not.

If they did, it is certain that the price of silver would for the moment rise, because so very large an extra quantity would at once be required; and it is very possible that this price might not again fall. The final regulator of the price of silver is, the cost at which it can be produced in the least fertile mine that can maintain itself in working. At the present moment, there are new mines as to whose extent there are very various accounts, which may supersede some of the worst of those at work, and so lessen the maximum cost of the production of silver,—the cost which fixes its price; but if so large a new demand for silver as that for supplying the United States with money were added to the existing demands, very possibly the extra fertility of these new mines might be exhausted before that demand was satisfied. These mines might come to be not so much better than the old mines as to throw any old mine out of work; and if so, the price of silver would remain what it formerly was. And if this happened, silver would be as good a standard of value as it has ever been.

There would undoubtedly be several difficulties in the adoption of a silver standard by the United States:—

First, much of the interest of their debt is now payable in gold coin. This would not, however, cause

much difficulty, if the price of silver were to rise, as we have suggested, to something like the old level. The United States might then either continue to receive their customs duties, as they now do, in gold only, and to pay their interest with such gold, or they might pay an equivalent in silver. The difficulty would be one of detail only, and might be met.

Secondly, — what is more serious, — the trade between the United States and the gold-using countries would be liable to be disturbed by every fluctuation in the value of gold and silver; and we are not yet in a position to say what the amount of this inconvenience would be, because the changes in the relative values of the two will in future probably be greater and more frequent than they used to be. As we have explained, the double-standard nations used to equalize the price for the rest of the world, and now it seems probable that they will do so no longer. An element of uncertainty would thus be introduced into the largest international operations of the United States, which might be very important, and which it is difficult to estimate beforehand; but in all likelihood this uncertainty would not be so great as that caused by the inconvertible and ever-fluctuating greenbacks which the United States have now borne very patiently for many years.

Thirdly, the United States will, by choosing silver for their money, undoubtedly suffer by using the less convenient metal for large transactions instead of the more convenient, — silver is bulky to carry and cumbersome to count: but a good and secure system of paper money might easily be devised, which would reduce this disadvantage to minor proportions; though that system, like all systems of paper money, is liable to the objection that it may be at any moment departed from, and a bad paper money substituted for a good. No nation which is engaged in first-rate commerce should select a silver money, unless it believes that its circumstances, the

character of its people, and the peculiarities of its government enable it to manage a paper one.

The great reason for inquiring whether it would not be best for the United States to take silver as a money, and not gold, is, that it is much more likely to be done. It is always a great advantage to have a strong private interest concurring with and enforcing a great national interest: and here the silver producers are anxious to sell their silver, and fearful that they may not be able to do so; whereas the gold producers, on the other hand, feel sure of their market, and are careless what happens. The fear is, that the United States may go on for many years to come with inconvertible paper, as they have for many years past; the difficulties of resuming specie payment are very considerable, and when resumed it may not be kept to unless it is some one's interest that it should be so. But the silver producers are clearly strong in Congress, wish to get their silver substituted for greenbacks, and would be watchful to see that, owing to keeping too small a reserve or other mismanagement, greenbacks did not come back again if they had once been got rid of. And these producers can put the argument in a way very attractive to American nationalism; they can say, "If you use silver you will raise its value, not only here, but throughout the civilized world. You will support an interest which needs supporting; and you will hurt no one, but make America richer, by so doing." And all nations — especially nations which govern themselves — are apt to be much moved by such reasoning.

We hope, therefore, that the American commission will not be distracted by the old phases of the currency question; and that they will give their attention to the new points presented by the present new relation between gold and silver, and the respective advantages and disadvantages of the courses they have to choose from. There is not one of them

which has not much of both; and in such case, only very deliberate study can show how to bring out the most good with the least evil.

XII.

THE PERMANENT EFFECT OF AN INCREASE OF "COUNCIL BILLS" ON THE FLOW OF SILVER TO INDIA AND UPON THE INDIAN EXCHANGES.

[From the *Economist* of Oct. 7, 1876.]

THE depreciation of silver and its effect on the Indian exchanges have been much discussed, and with the best result. The Indian government, we are glad to say, have announced that they would adhere to right principles, notwithstanding the greatness and suddenness of the difficulty in which they are placed, and the number of wrong schemes obtruded upon them. But another fact, of which the practical effects are inextricably intermingled with those of this depreciation, — the recent great increase of the political payment of tribute which England derives from India, — has not been studied with equal care. It appears from the investigations of Mr. Goschen's Committee that the "Indian Council" bills, which represent that payment, have increased in the last ten years as follows: —

Year.	Bills of exchange drawn on India. £
1865–66,	6,998,899
1866–67,	5,613,746
1867–68,	4,137,285
1868–69,	3,705,741
1869–70,	6,980,122
1870–71,	8,443,509
1871–72,	10,310,339
1872–73,	13,939,095
1873–74,	13,285,678
1874–75,	10,841,615
1875–76,	12,389,613

It appears also from the same authority that most of the effect which this great increase in the payment from India to England might be expected to have upon the exchanges, was delayed by a simultaneous increase in the payments made from England to India. Till quite recently we have been very largely investing capital in railways and other public works; the funds necessary for these were raised in London and were sent out to India, and so compensated for the increase of the tribute. But now there is no longer any equal transmission of capital to India, and we therefore for the first time feel the effect of that increase.

The immediate result has naturally been, to counteract the flow of silver to the East. When commerce is left to itself, the imports England takes from India are much greater than the imports which India takes from England, and a part of the balance has to be paid for in specie; the rest being settled in indirect ways, of which we need not speak now. But the increase in the "Council bills" provided a competing remittance with silver; if a merchant wanted to make a payment in Calcutta, he had the choice either to buy bills or send out silver, and of course so much less silver was sent.

The effect was the greater because the government of India must bring their money home from India, and therefore must sell their bills; whereas "silver," like any other commodity, may go to many markets, and may be held when its price falls. This is the reason of the saying, "The price of Council bills rules the price of silver, not the price of silver that of Council bills:" it is the price which the more anxious seller must accept that for the moment predominates, and not that which the less anxious can wait for.

So far all is clear, and has been well discussed; but what has not been equally discussed is the question, Will this effect be permanent? How far will

the increase of its political payments prevent India from obtaining silver, which is the material of its money? and if it ceases to have this effect, why does it do so?

It clearly cannot have this effect always, or a country like India might be prevented, by an increase in the tribute which she has to pay, from obtaining money altogether. Suppose a dependent country obtains all her supplies of bullion from the dominant country to which she belongs, and that the dominant country imposes an annual tribute equal to the amount of silver which she annually takes: if the consequence of the tribute be, to prevent the export of bullion by an equal amount, the dependent country would cease to obtain money altogether, and prices in it would fall and fall indefinitely.

In fact, of course, this will not happen: because as soon as prices fall below a certain amount, an encouragement is given to the export and a discouragement to the import trade; and so a new adverse balance of trade is created, which will take bullion to the dependent country. The effects of the imposition of a tribute on the industry of a dependent country are two:—First, to drive away all cosmopolitan capital which can carry on its business elsewhere. It takes for the use of the government a certain portion of what used to be the profit of the capitalist; and if in any other country capital does not pay an equal tax, that large class of capitalists who now belong to all countries will go to some other, and will carry on their business there. And secondly, the residential capitalists, whom no motive will tempt away, must be content with a less rate of profit than they used to receive. Particular industries, for which the dependent country has special advantages, will to some extent be an exception: but as a rule the effect of the augmented tribute will be, to lower prices; because as a rule, and for almost all commodities, it will fix profits on a lower range.

A country which has a tribute to pay of £15,000,000 annually must send abroad annually £15,000,000 worth of commodities more than she receives; the profits of her various industries must be less by that £15,000,000; prices must be lessened to effect this; and (supposing, as is the case with India, that this country does not produce the precious metals) prices will be thus lessened by a corresponding reduction in the import of those metals.

Thus, in the case of India, the effect of her augmented political payments will be, to lower the level of prices till her exports rise above her imports by an equal sum. Till that level is reached, silver will not be sent from England; but when it is reached, silver will be sent at once. The effect of the augmentation, therefore, is not to lessen the export of silver from England to India permanently, but only to diminish it temporarily and till the course of commerce has adapted itself to the new circumstances. India will not indeed receive *quite* as much as before the increase of her tribute; she will have a somewhat smaller stock of silver to maintain in order to carry on her trade, as prices are lower (which means that less silver does the same work), and therefore the annual supply requisite to maintain prices at that level will be less: but this is but a very minor effect, which is not of much practical account; and except so far as its influence extends, the import of silver into India will eventually be as much, now that Council bills are £15,000,000, as it used to be when they were £5,000,000.

Some persons who have been much in contact with the recent phenomena of the silver market, but who have not considered the more permanent parts of the subject, will probably be surprised at this conclusion; but this is only one of very many instances in which a great familiarity with the momentary facts of a particular kind of business is a wrong

rather than a right guide as to what the course of that business in the long run will be.

It will be seen that the case of India is a very peculiar one. Not only is she politically dependent on England, but she derives her silver from hence too; the country which imposes the tribute, and thereby tends to take money, is also the country which supplies money. Ordinarily the imposition of a tribute on a subject country is much simpler in its effects: the dominant and the subject countries are only connected by the usual trading relations; coin and bullion only pass to settle the balance of trade, and in the long run pass about equally both ways. In this case the effect on the flow of bullion is, on the face of it, only temporary: there being no continuous export of bullion from the dominant country to be arrested, the question whether it will or will not be arrested does not arise. The dominant country simply takes a portion of the produce of the industry of the dependent, and so far renders it less profitable; the range of prices in the dependent country must necessarily be lowered to effect this end, and for a time the supply of the precious metals to it will be diminished: but upon its permanent import of those metals the imposition of the tribute will have no effect, — as soon as the proper range of prices is reached, the bullion trade will go on as usual. And so it is in the case of India also, though England's being the country which supplies bullion as well as that which imposes the political payment seems at first to make a difficulty; substantially the effect of the new tribute will be the same in this case as in all others.

But though the increase of the Council bills will not, as we have thus shown, change the quantity of silver sent to the East, it may have lasting effects on the Indian exchanges; and next week we will examine whether it has or not.

XIII.

THE EFFECT OF THE "COUNCIL BILLS" ON THE INDIAN EXCHANGES.

[From the *Economist* of Oct. 14, 1876.]

We proved last week that the effect of the augmentation of the political payment from India to England, shown by the recent increase of the bills drawn by the Indian Council upon India, will have no permanent effect whatever on the export of silver to India; the great influence which it has had in that respect will be transitory only. We have now to see whether the equally great effect which that increase has had on the Indian exchange will be equally temporary.

To simplify the subject, which is complex, let us first take the simple case of a dominant and a subject country which have the same currency, whose trade exports usually balance each other, and neither of which produces the precious metals, nor depends on the other for the supply of the precious metals. In this case, there being only one currency in the two countries, the quotations of exchange will be always made in their most intelligible form; that is, by the premium or discount on the bills which each country draws on the other. In this case, bills on the dominant country in the dependent, and bills on the dependent in the dominant, will as a rule be equally often at a premium. The trade exports from the ruler to the subject exactly equal those from the subject to the ruler; the bills generated by them will therefore be equal, and also the demand for means of remittance. There is no indebtedness between the countries to be settled, and so on the average everything will be even between them.

If this state of things is disturbed by the imposition of a tribute, the first effect is, that bills in the dependency on its superior rise to a premium; that

tribute has to be paid, and these bills are inquired for as the best means of payment. It becomes more difficult (as Indians would say) to "remit home," because there is more to be remitted, and no increase in the means of remittance. The premium will probably rise above the specie point, and coin or bullion will be temporarily sent to the dominant country in consequence. But it can only be so sent temporarily, for the dependency we are considering does not produce the precious metals. In time, therefore, some other means of payment must be found; the tribute must be paid not in gold or silver, but in other commodities. These commodities will begin to be exported as soon as that export becomes profitable; and that profit will consist of two elements: first, of the difference between the price of the commodities in the dominant country and the price in the dependency; and secondly, of the premium at which the merchant in the dependency can sell his bill. The imposition of the tribute will have caused both elements of profit: by producing an export of specie from the dependency, it will have lowered prices there; and by creating a demand for the means of remittance, it will have raised the price of the bills. There will, so to say, be a *bounty* on export caused by the state of the exchange; and the export will be made when the price profit, *plus* that bounty, are together up to the rate which the capitalist wants. Before that the export will not take place, but after that it immediately will.

And this state of prices and of the exchange will, except other causes interfere with it, tend to be permanent: there is nothing in the relation of the dominant and inferior country to alter either. Till the whole tribute is paid, both will as a rule continue in this condition: and if the tribute is an annual payment, every year the same causes will be at work and the same consequences will happen. The profit on the sale of the bill will more or less

help the price profit, and cause the operation to be made earlier than it would if the price profit only could be obtained.

The effect of this is, to enable the dependency to "get off," so to speak, and pay its tribute with a less alteration in the level of its prices than would otherwise have been necessary. In so far as the payment of the tribute is aided by the state of the exchange, it is in fact aided by a *loan:* the seller of the bill gains funds from the money market, which return to that market when that bill is paid. As the transaction is a continual one, always being renewed, the final result is, that the dependency pays a part of its annual tribute by a chronic floating debt, which the exporters of its commodities borrow, and from which it derives the benefit. And it will make no matter if the exports are shipped not directly to the dominant country, but to some third country to which the dominant country owes money: in the latter case, the country which receives the exports from the dependency pays for them by a draft on the dominant country, and that draft is taken as a payment of the tribute. The dependency pays the debt of the ruling country, and this is quite as good as the direct export of value to it.

And no part of this will in the least be altered by the fact that the two countries, the dominant and the dependent, use different currencies, if these currencies are both of the same metal, whether gold or silver. The mode of expressing the exchange by the equation between the coins is only a complex way of expressing the premium and the discount on bills at the moment. Two calculations have in such a case necessarily to be made in buying and selling a bill; the currency of one country has to be turned into that of the other, and the premium or discount of the bill to be ascertained: and for convenience' sake, in the common mode of quoting the exchange, the two computations are put together and their joint effect

told. But there may be a real temporary difference if the currencies are of different metals. If the metal of the currency in which the relative tribute is fixed, falls in value, the tribute is lightened; and if it rises, the tribute is made heavier: and this will affect prices and the exchange, just as an increase or decrease of the tribute in any other way; but the principle of the argument is unaffected.

Nor is that principle really changed if the dependency, like India, receives its supplies of the precious metals — that is, of money — from the dominant country. In that case, before the tribute is enforced, the exports from the dependency to or on account of the dominant country will be greater than its imports from it; bills in the dependency drawn on the dominant country will be in general at a discount, and those drawn in the dominant country at a premium. There will be a greater facility of remitting money from the inferior to the superior country than, *vice versa*, from the superior to the inferior; and therefore when the tribute is imposed, the new demand for remittance, so created in the inferior country, will have "some leeway" to make up. Finding bills at a discount, it will have to go on till it makes them at a premium. It will have to stop the flow of specie to the dependency; and if this is not enough to reduce prices, it must go on till it turns the tide the other way, and sends bullion, contrary to its natural course, back from the dependent to the dominant country: but it cannot permanently have this effect, because, as we have seen, the supplies of bullion will in the long run be the same after the imposition of the tribute as before it; the exchange will settle down so that the usual amount of bullion will pass. But subject to this, the consequences will be the same as before: bills in the dependencies will not be so often or so much at a discount as they would otherwise have been, or bills in the dominant country so often or so much at a premium; and the exports from the

dependency, which used to be depressed by that discount, will be less depressed, and the exports from the superior country, which used to be encouraged by that premium, will be less encouraged. But the final effect will be the same: the adjustment of prices and the adjustment of the average exchange taken together will be such as to cause the imports from the dependency to the dominant country to exceed, by the extent of the tribute, those from the dominant country to the dependency (specie included). The tribute will be paid in an excess of value consigned from the dependency to or on account of the dominant country above that consigned the contrary way. In so far as that result is attained by a change in the premium on bills, and not by a change of prices, the dependency is enabled, in this case as before, to pay its tribute by an exportation of fewer commodities than it would otherwise have to export. It obtains a loan to that extent from the money market, just in the same way and just with the same effect as before.

The last case we have been considering is that of India exactly; and it therefore appears that though the increase of the "Council bills" will have no permanent effect on the export of silver to the East, yet it will have a considerable effect on the value of the rupee as quoted for exchange, and that it will tend to make remittances from England to India easier, and from India to England less easy, as long as it continues.

XIV.

THE MINUTE OF THE INDIAN GOVERNMENT ON THE DEPRECIATION OF SILVER.

[From the *Economist* of Oct. 28, 1876.]

THE Minute in which the government of India have replied to the petition of the Bengal Chamber of

Commerce that they would suspend the coinage of silver for private persons, is a very able document. It shows with admirable clearness that the effect of the plan proposed by the Chamber would be to give the rupee an artificial value, to lower prices, and to disorder trade. It observes that

"It is essential to a sound system of currency that it be automatic. No man or body of men can ascertain whether, at any particular moment, the interests of the community as a whole require an increase or diminution of the currency; still less, how much increase or how much decrease is at any moment exactly needed. No government which aspires to keep its currency in a sound condition would be justified in attempting that impossible task; or in leaving the community, even for a short interval, without a fixed metallic standard of value. Under an 'open-coinage system,' these things regulate themselves without official interference."

And on this ground it declines to become the sole coiner of rupees in India, and says that the amount of the silver coinage must be left as before, to the action of the Indian people, who are the best judges of their own wants.

The Minute shows also, by a careful review of all the circumstances, that there is (at any rate as yet) no reason for a change in the Indian currency; as no one can yet say what will be the value of silver, either as compared with gold or with commodities. As has been abundantly proved in this country, no action in the matter is at present required of the government of India; and by far the preponderant probability is, that no action will ever be required of it.

The newest, and to us the most interesting, part of the Minute is that which is devoted to explaining that, in the judgment of the Indian government, it is not yet proved that there is any depreciation at all, certainly not a depreciation to the extent which is commonly believed: —

"The divergence now noticeable in the values of gold and silver does not necessarily prove a diminution in the value of silver. It may be equally well accounted for by a rise in the value of

gold; and in fact it is probable that, since the commencement of this divergence in November, 1872, there has been an increase in the value of gold as well as a decrease in the value of silver. The actual values, measured in silver, of general commodities, whether in India or in England, afford as yet no evidence of any recent, sudden, or violent fall in the value of silver; and if *a priori* considerations strongly indicate that silver must have fallen, such considerations also make it probable that gold must have risen in value. Appended to this resolution is a series of tables of prices in London and in India, the information contained in which points to two conclusions: first, that gold has risen in value since March, 1873, and especially since last December*; secondly, that it is not shown that silver has fallen in value — *i. e.*, as compared with commodities in general, either in London or in India — during the same period. These conclusions are open to correction on a wider review of the economical causes which have been at work during the period; but they appear to indicate a rise in the value of gold as at least one of the causes which have disturbed the equilibrium of the two metals. The bearing of both conclusions upon the questions now before the government of India is important."

As far as gold is concerned, the tables which are given by the government are ostensibly those which we have often laid before our readers. It is undeniably true that the gold prices of commodities are as a rule less in 1876 than they were in 1873; and in this sense it is true that gold has appreciated, as against commodities. But then it is equally true, and equally shown by the figures of the Minute, that the gold prices of commodities were more in 1873 than they were in 1869 or 1870; and if we are to say that gold is *ap*preciated now as against 1873, we must by parity of reasoning say that it was *de*preciated in 1873 as against 1869. In fact, as all our readers are aware, 1873 was the culminating point of one of the rising periods of price, just as 1869 was the lowest point of the falling period. We wrote on the subject at the time, — on Jan. 4, 1873: —

The main cause of these cycles in price and trade is, as we have often shown, the different amounts of loanable capital which

* *I. e.*, December, 1875.

are available at different times for the supply of trade. After great panics like 1847, 1857, and 1866, for a very long period enterprise is so slack and credit so bad that there is no possibility of employing an increasing capital to advantage. Trade continues much as it was, whereas the savings of the country are accumulating constantly. Accordingly, there is at such seasons a constant excess in the supply of loanable capital over good bills and other accredited securities; the rate of interest, which is the barometer of the relative supply of these articles, continues very low generally through a series of years. After a certain period, some circumstance more or less powerful occurs to augment trade; and then the effect of that capital is felt. Enterprise revives as credit grows, and that capital is lent largely. Till some stimulating event happens, experience shows that such capital may lie almost idle, and that in consequence for years the rate of interest may continue long very low. Bankers — the principal holders of that capital — do not and cannot manufacture securities; they remain quiet and passive till securities of what they consider a substantial kind are offered to them. But when from some cause peculiar to itself trade does revive, bankers are only too eager to lend; and trade, so far from wanting the money which it requires, finds the accumulated capital of bankers lying ready and waiting to be used by it. The development of one trade, too, is never isolated. If any one great industry — say the iron trade — starts into sudden prosperity, the purchasing power of all persons connected with the iron trade is largely augmented, and all the dependent trades, and all the trades in which those concerned in the iron trade lay out their money increasingly, thrive in consequence; and these second and dependent trades quicken other third trades dependent on them, and so on through the industrial world. The first period of every industrial cycle is a period of immense new production, and of great prosperity running through and permeating all trades.

This period is also one of very high price. The loanable capital — the deposits which have accumulated in the years of depression are then poured into trade. These have the effect of new money: they are a new purchasing power, which augments all prices dealt in, and especially the prices of wholesale articles, which are those upon which enterprise most acts, and in which speculation is quickest and most constant. Experience shows, too, that the rise in prices so produced is a cardinal element in every investigation of the value of money. The effect of the Australian and Californian gold cannot, as Mr. Jevons was the first to show, be even tolerably

investigated unless this periodical cause of elevation in price is first eliminated, and its effects separately set aside."

And in the same way now, we must be careful not to confound this sort of appreciation of gold with that which would arise from a diminished production consequent on increased difficulty of attainment. This last would have a tendency to be permanent, — at least, to last as long as the increased difficulty of attainment lasted: but the appreciation which is part of the cycle of prices is sure not to be permanent; it is only a passing incident in the mercantile world, and is sure to be followed by an equal depression.

It may be said that the present appreciation of gold is due to the new demand for it in Germany and elsewhere; but this demand tells two ways. What we are comparing is the high range of prices in 1873 as compared with the low one in 1876; and one of the effects of the German demand for gold in 1872 and 1873 was, to make the rate of discount often much higher in Lombard Street than it would otherwise have been, and so to reduce the prices of all commodities which rise in the speculative times. If it had not been for the German demand for gold, the range of prices in 1873 would have been higher than it was. We cannot, therefore, attribute the fall in prices since 1873 to that demand; for it was then already producing a great effect, — a greater, indeed, we think we could show if necessary, than it ever did afterwards.

The gold price of silver has now been affected in the same way as the gold price of other commodities for the first time, because it has been now for the first time a commodity in the same position as other commodities. Formerly, the existence of a "double standard" in various important countries took off from the market, part of any sudden extra supply of gold or silver, replaced it by an equal supply of the other, and so equalized the price; but now that the "equilibrating apparatus" has been withdrawn, the

price of silver in gold upon the London market will be affected by the causes which produce cycles of price, just like anything else. How far in this case it has been so affected it is difficult to say, because we have no experience. All commodities are not equally affected by these cycles; some are more so, some less, and we cannot say beforehand what will be the effect on any one. The causes which determine this are too many, and their proportions too unknown, for *a priori* reasoning.

But as far as we can judge, we should not be disposed to attribute so much effect to this cause as the Indian government would seem, from the prominence they have given to it, to be inclined to do. So long as silver is largely used as a currency by many countries, it is likely to be a commodity superior to the average of commodities in stable value. All currency commodities, so to speak, are so: their efficiency in exchange diminishes with any decrease in their value, and a greater quantity of them is required; in no other kind of article does a fall in price generate so large an increase of demand, and therefore so much tend to be its own cure. We should therefore expect silver to be ordinarily much less affected by the causes making "cycles" of price than other commodities.

The figures contained in the table attached to the Minute confirm this view. They show that, taking the prices of each article in March, 1873, as 100, the price of the following articles in the London market was:—

PRICES IN LONDON OF CERTAIN COMMODITIES IN MARCH, 1873, COMPARED WITH APRIL, 1876.

	March, 1873.	April, 1876.
Beef, inferior, ...	100	110.00
Coffee, ...	100	95.37
Beef, prime small, ...	100	104.76
Silver, bar, ...	100	89.54
Copper, Chili bars, ...	100	88.27

	March, 1873.	April, 1876.
Flour, town made,	100	86.17
" New York,		83.20
Wheat, American red spring, at N. Y.,		90.06
Wool, South Down hogs,	100	80.48
Saltpeter,	100	80.18
Cotton, No. 40 mule twist,	100	80.35
Wheat,	100	81.90
Pepper,	100	64.77
Sugar, foreign Muscovado,	100	71.79
Cotton, middling uplands,	100	68.92
Coals, Hetton Wallsend, London,	100	63.43
Sugar, Mauritius,	100	69.08
Straits tin,	100	49.14
Scotch pig iron (warrants),	100	49.19

From this we see that silver has not, in matter of fact, changed as much during the time we are considering as many other articles. And upon the whole, the well-known causes tending for the moment to depreciate it—the extra supply from Germany, the want of demand from the "Latin Union," and the apprehension of the new mines—seem to us, as far as we can measure them, causes of a far greater probable effect than the cyclical causes, as far as they affect silver. The utmost we should be inclined to say is, that the cyclical causes produced a weak market, and that the effect of the other causes was in some degree aggravated by this weakness. We believe the special causes affecting silver to be those to which its depreciation is principally owing, and that the causes acting on the value of all commodities only in a minor degree contributed to it.

We are not indeed sure that the Minute was meant to claim for the appreciation of gold more than this subsidiary effect; but the prominent place which is given to it might mislead unwary readers into thinking otherwise. As a whole, both in its conclusions and its reasonings, the "Minute" is most admirable. India is singularly fortunate in having rulers so well able to understand and to cope with a difficulty so peculiar and so little expected.

XV.

A PROPOSED REMEDY FOR THE DEPRECIATION OF THE SILVER COINAGE OF INDIA.

[From the *Economist* of Nov. 11, 1876.]

It has been suggested that the coinage of rupees should be suspended in India; that their importation should be prohibited; that gold should be coined for any one who will take it to the mint at a fixed rate (say at 2*s.* the rupee); that both rupees and gold should be legal tender, which every one must accept, but that for the present, at least, no one should be able to demand gold. And in this way it is hoped that a gold standard would be introduced into India, without the Indian government having to buy gold to exchange for silver, the cost of which would be more than it could afford.

But when examined, it will be seen that this is a plan not for introducing into India a gold standard, but a double standard of a peculiar sort. Though the coinage of rupees is suspended, they are still to be legal tender, and their value will therefore continually rise; they will be "monopoly coins," so to speak, circulating at a scarcity value, and they will so circulate concurrently with gold. And this is to be the perpetual currency of India,—for the only motive for thinking of it is, that silver is already about to fall greatly in value; its very adoption would for a very long time cause such a fall, because it would close the Indian market against silver, and therefore the cost of buying gold to exchange for the rupee currency of India will be, years hence, more insuperable than it is now.

But to this plan there are the gravest objections.

First, a currency of "monopoly coins," circulating much above their cost value, is sure to cause their forgery; this is as certain as that a high tariff will cause smuggling. If silver should fall enough to

make this scheme worth thinking of, the gain by coining rupees in India, or importing them into India, would be very great, and we may depend upon it capital would go into the business. Some of the shrewdest people in the world — the American producers of silver — would have an interest in managing it, and we may be sure they would manage it. The case must not be confounded with that of a "token coinage" of silver, such as we have in this country; because our silver coins are only legal tender for small sums, and therefore great masses of them are useless. But in the plan supposed, "monopoly coins" would be the main currency of India, and any quantity of them could be got rid of. India would seem to have most unusual facilities for the operation, for there are native states embedded in our territory where we hardly know what happens, and there is a rich monetary class of shroffs and bankers who would feel no effectual moral scruple against disposing of illicit rupees. The moral objection to such a currency as one of perpetual use is very great; for it is an incessant temptation to diffused fraud, and this evil would be fastened on India forever.

Secondly, the confusion in trade it would cause would be extreme. Suppose it were now enacted that no more rupees should be coined, and that gold should be coined at 2*s.* the rupee, the export trade from India, now stimulated by the low exchange, would be stopped, for the exchange would gradually rise; nor for a time at least would the import trade into India find a corresponding gain, for a great uncertainty would be produced, in which no new business would be created, though old business would be stopped.

Thirdly, this would deprive India of the great advantage she will gain, if the present state of things continue, as the *entrepôt* through which silver is introduced into the East. This is always the effect of a lowered value of the currency metals. The first

persons who get them from the mines gain much; those who buy them from the mining people gain much too; and so on, till the depreciation is effected. In the case of India, the importation of silver will gradually raise silver prices; this will bring imports into India from other countries where they have not risen. For very many years England has in this way derived the greatest advantage from being the first country to which the Australian gold was sent, and from which it was diffused. The Indian Finance Minister is no doubt troubled by the fall of silver, because he has to buy gold in London; but India itself will probably be benefited by it, for it would give her an easy money market and an extending trade for exports and imports, which the suggested scheme would spoil.

Fourthly, the currency so introduced would be a very bad one. There would be one currency fit for foreign payments,—the gold,—and another not so fit. The "monopoly coins" would be unexportable; and so when any one wanted to make a foreign payment he would have to get gold, which as a rule would make gold at a premium. The effect would be just like that of a plan often discussed formerly in England; viz., making the notes issued on securities by the Bank of England (the £15,000,000) inconvertible, the rest remaining convertible. The "monopoly" rupees would be of limited number and artificial value, just like the security or government notes we used to discuss; and their effect would be exactly what Lord Overstone predicted in 1857, in his evidence on Bank Acts:—

"Our affairs would then go on very much in the way that a man would walk with one of his legs six inches shorter than the other. One set of notes would circulate at a depreciation compared with the other set of notes; hence great inconvenience and confusion would arise.

"4050. What would be the real effect of it?—The effect would be, that you would have paper money of two different characters in the country, not of equivalent value,—not circulating

indiscriminately each for all purposes, but some useful for one purpose and some useful for the other; and that there would be intolerable confusion. A man would have government notes, and he would present them to another man in payment; that man would say, 'I do not want government notes: I want to make a remittance abroad; I cannot get bullion for those government notes; I will not take them.'

"4051. Are they both to be a legal tender? — They would both be a legal tender as far as the government is concerned, but the government note would not be a legal tender between individuals. Then what is that individual to do? The other man says to him, 'You must go and get me the other notes. Either you or I must pay a premium for them.'

"4052. What would be the harm of that? — The harm would be, enormous injustice and intolerable confusion."

In the plan now suggested, — monopoly coins being compulsory tender, gold not being demandable, — it would be settled which party should pay the "premium"; everybody would be obliged to take the purely domestic medium of exchange, and to buy with it the medium which is also of foreign use: but in other respects the evil would be exactly what Lord Overstone describes. There would be two currencies in the country, with different values; and prices in one would, as far as the discrepancy went, be different from those in the other.

For a short time, and during a period of transition, we can quite imagine that this inconvenience might be endured. But the present plan is by its essence a permanent plan, — a plan for making a currency for India for all time; and then an inherent effect* of great magnitude, such as this, becomes a most grave objection. As Lord Overstone said of the old plan: — "Then you would have a certain proportion of the monetary system of the country circulating at a discount; I cannot conceive a greater state of monetary disorganization than that."

No doubt it is said that the Indian government may "regulate" the currency, — that it may withdraw

*An evident slip for "defect. — Ed.

rupees from circulation, that it may add to the gold in circulation, and so equalize the value of rupees and gold; but to succeed in such an attempt, the Indian government would want to know the amount of currency required for foreign payments, — which is that which causes the difference between silver and gold, — and this they never could know. And American experience of "gold sales" and greenback withdrawals is a great warning against giving any government the power of arranging the currency. It is sure to injure the good repute if not the real good faith of the government (for it necessarily creates pecuniary secrets of great value); and nevertheless it is not at all sure to attain its end, and to equalize as is intended the two kinds of currency.

For these reasons, we cannot think that the suggested plan for a new Indian currency would be a good one, even if it could be shown that silver was sure to be permanently excessively depreciated; and as the preponderating probability seems at present to be that it will *not* be so depreciated, we are still more of opinion that it would be unwise to begin a policy on the face of it, and almost admittedly, so anomalous.

XVI.

THE TRANSITION STATE OF THE SILVER MARKET.

[From the *Economist* of Dec. 9, 1876.]

THE delicacy of the silver market at present is curiously illustrated by the course of the price of silver in the London market this year: first there was an immense fall, and now there has been an equivalent rise. The figures are —

				d.		d.
In 1876	the fluctuations in	January	were between	$56\frac{1}{8}$	and	$54\frac{7}{8}$
"	"	February	"	$54\frac{7}{8}$	"	53
"	"	March	"	$54\frac{1}{4}$	"	$52\frac{1}{2}$
"	"	April	"	54	"	$53\frac{1}{2}$
"	"	May	"	54	"	52
"	"	June	"	52	"	50
"	"	July	"	$51\frac{1}{2}$	"	$46\frac{3}{4}$
"	"	August	"	$53\frac{3}{4}$	"	50
"	"	September	"	$52\frac{9}{16}$	"	$51\frac{1}{8}$
"	"	October	"	$53\frac{1}{2}$	"	52
"	"	November	"	55	"	$53\frac{1}{8}$

Present price, Dec. 10, $56\frac{1}{4}d.$

Such rapid changes of so great a magnitude could only happen in a very delicate market, where a little extra supply (or even only an apprehension of an extra supply) will at once send down prices, and where a slight extra demand (especially when it seems at all likely to be permanent) will at once send them up. The delicacy in this case has been due to the fact that the silver market is now in an entirely new state; and that until the conditions which regulate that state are discovered, all dealers are fearful of keeping any considerable amount on hand. They sell what comes as it comes, which sends down the price; and in consequence they have none to sell when there is a sudden demand for an extra quantity, and therefore the price rises.

In former times it was not necessary to keep a stock of silver, and there was no motive for it; for the "Latin Union," being a collection of countries with a double standard, held an immense stock for all the world. If silver showed a tendency to rise in price, gold immediately was sent to purchase it in the country where it could be obtained at a fixed price in gold; and similarly, any stock of silver which accumulated here was carried off to the "Latin Union" as soon as it had the least tendency to depress the price. Much silver could not be kept in stock, and there was no motive for keeping any. But

now this peculiar organization has ceased to act, for the "Latin Union" has practically ceased to be a "double-standard" league; because it does not coin, and therefore does not take new silver in indefinite amounts when required.

The silver market will therefore in future, like all other markets, have to secure its stability by keeping a "stock on hand." Dealers will hold for what they think a good price, which will usually prevent an extreme fall of price; and get rid of more or less of this accumulation when there is an unusual demand, which will commonly prevent an extreme rise. But a great number of causes as yet prevent the dealers from doing so. First, the uncertain quantity which the German government may at any time sell, hangs over the market; the effect of the increase of the "Council bills" on the Indian demand for silver has still to be fully tested in practice, — indeed, it will require years so to test it; the American production is still an unknown quantity, though everything seems to show that it will be much less than it was thought to be; the "Latin Union" is still in an "expectant attitude," and may possibly resume its old policy. Till these causes have ceased to operate as powerfully as they now do, no important stock of silver will be kept, since the future is too uncertain to justify it; and until it is kept the price will probably fluctuate a good deal, — though not as much as during the past year, when most of the influences that cause variation have been at a maximum, and most of those which cause stability at a minimum.

The rise in the price of silver which has just taken place is as local as the fall which preceded it; the great mass of prices in the countries using silver as a money are wholly unaffected by it. Indeed, such perturbations as a rise of 20 per cent., and then a fall to the old level, during a single year, in the general prices of great countries, would have been economical phenomena such as the world has never

seen, and such as would have caused a vast derangement of transactions.

The silver market must settle down into its normal condition before we shall know what will be the normal price of silver in relation to gold or to commodities. The disturbing forces with which we have had so long to deal must first pass away; and until they have so passed, it will be desirable that no government shall involve itself in a currency change, depending on the mutual relations of silver and gold, which has not begun one already. Unless in case of vital necessity, such currency changes should be made at the time when the circumstances attendant on them can be best foreseen; and that is when the course of trade is most regular, and the chief markets in the matter most in their normal condition

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XVII.

BIMETALLISM.

[From the *Economist* of Dec. 30, 1876.]

We have written much this year on the subject of silver, and on the evils of its depreciation; but we have hardly, we think, referred to the scheme which some persons think would set right everything, — the scheme of universal "bimetallism." But the truth is, that we regard that scheme as so entirely beyond the boundaries of practical finance that we did not think it worth discussing; and we only discuss it now because we continue to receive ingenious pamphlets, some of them written by men of business, which maintain that it is both practicable and advisable. We shall therefore state as shortly as possible our reasons for thinking that it is neither.

The plan is, that by means of an "international conference," or otherwise, all nations should agree to use both gold and silver as legal tender for all

amounts, and to use them in the same proportions; which, it is said, would cure any evils which now arise from changes in the relative value of gold and silver, and in the cost of production of both or either of them.

But first, any such attempt would be such an alteration in the monetary system of most countries that it would be difficult to get most of them to take it into consideration, and impossible to induce many of them to agree to it. Take our own case: England has a currency now resting solely on the gold standard, which exactly suits her wants, which is known throughout the civilized world as hers, and which is most closely united to all her mercantile and banking habits. What motive, that an English Parliament could ever be got to understand, is there that would induce them to alter it? You cannot even begin an argument which would seem to have a sufficiently striking sound. Some time ago it was indeed said that the finances of our Indian Empire were thrown into confusion by the fall in the price of silver, and that therefore the English and the Indian currency should be assimilated, and both be on the "double-standard" principle. But even in that case the English people would, rightly or wrongly, never have consented to change their currency: they would have told the Indian financiers to adjust their system of raising a revenue to the new circumstances; they would not have altered the sovereign for anything which might happen to the rupee.

And still less would the English people think of doing so when silver has risen in price, and when our Indian finance is no longer inconvenienced. They would say, with their usual untheoretical common-sense, "This event shows how dangerous it is to make great changes upon fine arguments in important matters. You — the advocates of bimetallism — wanted us to make a most troublesome and difficult change to cure our evil, which has now for

a time entirely, and perhaps forever, cured itself. We certainly shall be cautious how we listen to you again."

Then it is said that under our present system the fall in silver throws exchanges into confusion, which no doubt alters the course of trade. But practical commerce soon adapts itself to such changes; and a nation which at present has a good currency, and one which suits it, would be very foolish to make a change merely to keep the exchanges from possible fluctuation. And as we have often shown before, the fluctuations in the Indian exchange, which have hampered our export trade to India, are not by any means wholly due to the change in the price of silver: they are partly owing to the increase in remittances from the East for interest of debt, and on other accounts, the effect of which was long suspended, but now is fully felt. And as we have also often shown, though the trade *to* India is impeded by a fall of silver, our trade *from* India—our imports from thence are stimulated; the same cause which tends to impair the one tends equally and necessarily to add to the other. A change in the monetary system of any one country can rarely be effected, except to prevent some great evil; a change of the system of a very large number of countries could only be made to meet some superlative evil: and in this case neither exists.

Most advocates of "bimetallism" now admit that unless all countries adopt it, and unless all countries keep to it, it is a very faulty system. It is not a currency of two metals, but an alternative currency, sometimes of one and sometimes of another; countries with such an alternative currency always use the cheaper metal and sell the dearer metal. Creditors in it are always injured, by being paid in the cheaper metal; debtors are always benefited, by being enabled to pay in it. The currency of France was thus a few years ago changed from gold to silver, and would now have been changed back again to

gold, if it had not refused to take the silver, and had not in so doing practically abandoned the bimetallic system. And a system which requires that every one should agree to make it good is certainly a system which is difficult to make good, and which is always liable to become bad.

And even if this system was at once, say by "miracle," imposed on all the human race, it would be very imperfect. It forces an arbitrary equation, in which there is no naturalness, between gold and silver; but their natural relative price has varied exceedingly. The following table, published by Mr. Goschen's Committee, shows this clearly:—

Date.	Ratio.	Authority.
A.D.		
1526	11.30	Apparent relation of market value as deduced from the British Mint regulations, some absurd and unsuccessful experiments in coinage being disregarded.
1543	11.10	
1561	11.70	French Mint regulations.
1575	11.68	
1551	11.17	German Imperial Mint regulations.
1559	11.44	
1604	12.10	British Mint regulations; experiments disregarded.
1612	13.30	
1619	13.35	
1623	11.74	Upper German regulations.
1640	13.51	French Mint regulations.
1665	15.10	
1667	14.15	Upper German regulations.
1669	15.11	
1670	14.50	British regulations.
1679	15.00	French regulations.
1680	15.40	
1687–1700	14.97	Ratios calculated from the biweekly quotations of the Hamburg prices current, giving the value of the gold ducats of Holland in silver thalers, down to 1771, and after that in fine silver bars. The nominal par of exchange during this period was 1:14.80, and the quotations show the variations of the market rate in percentage above or below this. At par, six silver marks-banco were equivalent to one ducat, $68\frac{20}{47}$ ducats containing one mark (weight) of fine gold, and $27\frac{3}{4}$ silver marks-banco containing one mark (weight) of fine silver. Hence, 6 multiplied by $68\frac{20}{47}$, divided by $27\frac{3}{4}$, equals 14.80, the par ratio.
1701–1720	15.21	
1721–1740	15.08	
1741–1790	14.74	
1791–1800	15.42	
1801–1810	15.61	
1811–1820	15.51	
1821–1830	15.80	
1831–1840	15.67	
1841–1850	15.83	

And the effect of the bimetallic system, if universal, would be, to fill the world with the cheaper metal only. That which could be brought to market most easily would come to market; that which could least easily be brought to market would not come: and there would in consequence be an incessant tendency to change of prices. No doubt that tendency would be impeded by the magnitude of the stock of the precious metals which now exists, and of which it would have to change the value; but still it would exist, and would be a constant evil.

But this and other characteristics, whether for good or evil, which may belong to universal bimetallism, are in our judgment scarcely worth considering; they seem to us fit only for theoretical books: because the plan is only a theory on paper, and will never be in practice tried.

APPENDIX.

EVIDENCE BEFORE THE SELECT COMMITTEE ON DEPRECIATION OF SILVER.

MONDAY, MAY 8, 1876.

MEMBERS PRESENT:

MR. BAXTER.
MR. CAVE.
MR. CHRISTOPHER BECKETT DENISON.
MR. FAWCETT.
MR. GOSCHEN.
LORD GEORGE HAMILTON.
MR. HERMON.
MR. KIRKMAN HODGSON.
MR. HUBBARD.
MR. MASSEY.
SIR CHARLES MILLS.
MR. SHAW.

The RIGHT HON. GEORGE JOACHIM GOSCHEN, *in the Chair.*

MR. WALTER BAGEHOT *called in and examined.*

CHAIRMAN.

1361. You have been for many years, I believe, the editor of the *Economist?* — Yes.

1362. I think you have given particular attention to this silver question? — Yes.

1363. Have you considered the relation between the depreciation of silver and the Indian exchanges? — I have devoted a certain amount of attention to it; and it appears to me to be almost certain that the first immediate effect of the depreciation of silver will be, to cause an unfavorable balance of trade with the East, and in consequence a great export of silver to the East.

1364. It has been alleged that the depression of the Indian trade has in part contributed already to the depreciation of silver? —

I should hardly like to give an opinion on such a point without reading the evidence which has been given before this Committee, which I understand has on this head been contradictory. It appears to me that to a great extent the depression in the trade has been common both to exports and imports, and therefore would not affect the balance of trade, or in consequence the exportation of silver to the East.

1365. If the fall in the value of the crops exported from India to England had been compensated by a corresponding diminution in the exports from England to India, trade might be depressed, but the price of silver would remain unaffected? — Quite unaffected, as far as that goes.

1366. Do you share in the view that has been expressed, that the drafts of the Council of India have contributed considerably to the depreciation of silver? — I should rather put it in this way: that the drafts in India represent an increase in the tribute — a beneficial tribute, no doubt — which India pays to this country; and of course that, being a payment which she has to make, alters the exchange, tends to make it unnecessary to remit silver from this country, and therefore diminishes the demand for silver.

1367. Do you believe that the fall in the price of silver has operated unfavorably, or is calculated to operate unfavorably, on Indian trade, either temporarily or permanently? — I should say that the effect of the depreciation of silver was, to cause an increased export of goods from India to this country, a diminished export from this country to India, and in that manner to cause an unfavorable balance of trade.

1368. Could you explain that a little more fully to the Committee? — I think the increase of the export of goods from India to this country will arise in this way: — A merchant in London, who is thinking of importing goods from the East, looks at the price current in Calcutta, and he sees the price quoted in rupees. The merchant in London is in possession of sovereigns in London, therefore he has two operations: first, he has to buy his rupees in India; next, with those rupees he has to buy the article which he saw in the price current. The question of profit and loss to him is compounded of the result of those two operations; if therefore he can buy his rupees in Calcutta on more favorable terms, he will find it to his interest to go into a speculation which would not otherwise be profitable. If he can get rupees at 1*s.* 8*d.* instead of 2*s.*, and he can buy his goods in Calcutta with the same number of rupees, that is so much extra gain to him. Conversely, the English exporter of goods to the East will receive payment in rupees, and

he will have to sell those rupees; and if he sells them for a less amount of sovereigns, he will suffer a loss, and that is a discouragement to exporting from this country to India. The result of these two operations — of the encouragement of exports from India to this country, and the discouragement of exports from hence to India — necessarily is, an increase of the balance which this country has to pay to India, and consequently a flow of silver to the East.

1369. And is so far a counterbalancing element tending to raise the price of silver, as compared with the other causes which have been mentioned which might depress the price of silver? — Quite so; and I should say, a cause of even greater magnitude than any which tend to depress it.

1370. It is a rectifying cause? — A rectifying cause, and a rectifying cause of the first magnitude; because what I have said extends not only to India, but to all countries which have a silver currency. Those countries are the great majority of the world; the circulation of silver in those countries is something enormous, and to all those countries you will have to send a certain amount if the depreciation of silver continues. The quotations of prices in all those countries are made in silver; traders with those countries have to go through the operation both ways, as to exports and imports, which I have described, in silver. As to all those countries, there will be a bounty on exporting from them and a discouragement to importing into them; and in consequence, to every one of those there will be a flow of silver.

1371. In order that the Committee may thoroughly possess themselves of those particular points, do I understand you correctly that the operation is as follows: A depreciation of silver in India and the depreciation of the Indian exchange have the following effect: that a London merchant desiring to speculate in Indian produce will be able with his gold to buy a larger number of rupees; and that if the prices remain stationary in India, he will, having a larger number of rupees, be able to buy the exports of India at a cheaper rate himself, and therefore make a larger profit? — Yes, that is one side of the operation.

1372. And on the other side, that the exporter of goods from this country to India will realize, if the prices have not risen (which is the same supposition), the same number of rupees in India, but in turning them into gold he will find that the identical number of rupees will furnish him with a smaller amount of gold in return here for his outlay, and that therefore he will make a less profit? — Yes, that is exactly my meaning.

MR. FAWCETT.

1373. That opinion, though, is based on the supposition that as the depreciation of silver continues, the prices remain stationary, is it not? But very soon after the depreciation commences in those countries where silver is a standard of currency, the rise in prices will be exactly proportioned to the depreciation of silver? — When it is, of course, the encouragement is withdrawn.

1374. After all, the depreciation of a metal which is chosen for the standard of currency is measured and is marked by the rise in prices, — that is what "depreciation of money" means: if you say that money is depreciated 10 per cent., you mean that prices have risen 10 per cent.? — I do not quite understand the question you ask.

1375. If gold were depreciated in this country 10 per cent., it means that gold possesses 10 per cent. less purchasing value? — Yes.

1376. Or in other words, prices had risen to that extent? — Yes.

1377. The same way in India, where silver, not gold, is the currency; if silver is depreciated to a certain extent, prices must rise to the same extent: therefore your reasoning is based on a hypothesis which cannot take place in actual life? — No; I consider that it is based on the present facts. The purchasing power of gold over silver by the English merchants is at this moment increased, — gold will buy a great deal more silver than it used to do: but the silver prices of articles in Calcutta have not been affected; silver is not as yet depreciated in the East. It is only during the process of depreciation that my argument holds.

CHAIRMAN.

1378. When I asked you your opinion, I drew a distinction between a temporary effect and a permanent effect: the opinion you have stated, I understand you to mean, is, the temporary and first effect? — Yes; as soon as the depreciation of silver as respects the Indian commodities is equal to its depreciation as respects the gold of the English merchant, then the process which I have described is at an end.

MR. FAWCETT.

1379. What I understand is this: that for a time — it may be shorter or longer — during which the depreciation of silver may take place without affecting general prices, you have indicated the prices* which will exercise an influence to restore the value of silver to its former level of value? — The point I wish to make before the Committee is this: that all over the East the process I have described

*An evident misprint for "process." — ED.

will go on ; and that to depreciate silver 2 per cent. all over the East will require a vast amount of silver currency, because the region is so large. No doubt it will stop when the depreciation of 2 per cent., or whatever it may be, has been effected ; but that will take a long time.

CHAIRMAN.

1380. The first operation is such as you have described ; the next operation would probably be, would it not, that the prices of commodities in India would rise ? — Yes.

1381. While silver had been depreciated ? — Yes.

1382. Then in proportion as the price of silver rose, you would require a larger amount of silver to do the work than had been used before ? — Yes.

1383. That increasing need for silver to pay for the aggregate increase due to the rise in prices would be spread over a vast surface, in your opinion ? — Yes, that is my meaning.

1384. Namely, over the countries with the silver valuation in the East generally ? — Yes.

1385. The greater demand for silver during this process would tend to arrest the fall of silver, *pro tanto*, in your opinion ? — That would be a main cause, supposing other causes which tend to depreciate silver to have the effect which is supposed.

1386. In the first instance, prices might remain stationary for a short time ; then the flow of silver would take place to the country, owing to the encouragement to export and the discouragement of import ? — Yes.

1387. And when that was past, and prices rose to their level, so that there was neither that encouragement nor discouragement, the aggregate amount of silver needed for the commerce of those countries would have been increased ? — Yes.

1388. After a rise of price all over the East, due to the depreciation of silver, more silver would be required for carrying on the general trade of those countries than before ? — Yes ; to a very great extent.

1389. Have you at all calculated the surface covered by what is called the silver "valuation," as compared with that which is covered by the gold valuation ? — It used to be said until a few years ago that England and Portugal were the only countries where gold was the standard of value ; and there were certain countries which had a double standard, but those were not very many ; and all the rest were silver. Silver was the normal currency of the world, and from a natural cause ; because silver is a much cheaper metal and

is suited to those small transactions which constitute the bulk of the dealings of mankind.

1390. Have you examined the statistics which are available to the public with regard to the aggregate amount of silver and gold in various countries? — I have examined them, but I regret to say that I do not think they are of such value as to be made the basis of sound reasoning in such investigations as this. It appears to me that you neither know with certainty the present stock of silver in the world, nor are you able to estimate the probable augmentation of it; nor do you know the effect which any given percentage, say 10 per cent. on the stock, would have upon its value. The last part is a matter which has not even been discussed, I think.

1391. You would question, after all the study you have given to the subject, both the accuracy and the real substantial value of figures that go into the aggregate amount of silver and gold in the world, and the proportions of the metals to each other? — I do not believe they are worth the paper on which they are written. I do not consider that any one knows anything about them, or has the means of knowing.

1392. To resume the point of the effect of the depreciation of silver on the Indian exchanges, which is one point referred to this Committee, — can you treat that question as one of exports and imports between India and this country alone? I have heard a remark with regard to the effect upon other countries. — Of course it will be evident that if this country has to export silver to the East, it must buy that silver somewhere. That silver it will have to buy in America; and therefore a consequence of the new state of things will be, that the English exporters of goods to some parts of the world will be benefited. I do not say the English exporters of goods to America, for probably we shall not pay America directly. The nature of the trade between America and this country is, that America sends us directly a great deal more than we send her, and America buys in various parts of the world coffee and rice and tea and a variety of articles, and that the sellers of those articles draw upon England, and so the balance is struck; we shall have to pay America in some way for the silver, and we shall pay her by exporting to the countries from whom she buys some of those articles: and therefore, though it is perfectly true to say that the effect of the depreciation of silver may be unfavorable to the English exporter of goods to the East, yet it will be favorable to another class of English exporters, — that is to say, those who pay America.

1393. You mean this: that as the silver is to be produced, and

comes to Europe, or when it comes to Europe, it must be paid for by some means?—It comes here, and we must pay for it. We shall pay for it, not to America directly, in all probability, but by exporting goods to various parts of the world where America buys. She buys in Brazil, in Cuba, and in the East, and in France, and all those countries draw drafts upon England, and ultimately the account is settled in commodities.

1394. If America draws more Eastern produce in consequence of producing more silver, and therefore having something to sell which it can turn into commodities abroad, then a certain amount of new purchasing power is given to those countries from which it draws its exports?—Yes.

1395. And that purchasing power they may again avail themselves of in purchasing from this country?—Yes; such are the dimensions of our trade, that ultimately they come to buy of us. We are the great settling-house of the world.

1396. Have you examined the effect of the depreciation of silver upon our trade up to this date?—I cannot say that I have made such an examination of it as I should like to lay before the Committee, especially as I understand that contradictory opinions have been expressed upon it; and I should rather rely on the general principle I have stated, because the facts of a particular year are far more difficult to discover than the general tendencies which operate over a long period of time.

1397. There are so many disturbing causes in any particular year?—Yes; and it is so difficult to get at the precise facts of any particular year. Statements may be made as to depression of particular trades: well, what does "depression" mean? the traders will not come and show you their books. You ought to have a comparative statement of their profits in the period at which the depression is said to commence, and at the period of which you are talking: now, no such account is ever given in, and therefore you are dealing with a statement which you have no means of measuring or testing.

1398. Do I understand you rather to question the prolonged depression in the Indian trade?—I do not doubt that there is a great depression in the export trade from this country, and that that arises very largely from the causes of which I have been speaking. The depreciation of silver has necessarily caused discouragement to export to the East; the people who most call themselves the "Eastern trade" are the exporters to the East.

1399. Unless the manufacturers and producers in our manufacturing districts have got stocks of articles already manufactured for

India which they are bound to sell?—No doubt they will have to sell them practically at reduced prices; because they will sell them in rupees, and when they bring these rupees home they will yield less in sterling money.

1400. Still, if they are manufactured they would be likely to be exported?—Yes, and perhaps for other reasons. Some part of the export trade—I would not at all say it is true of the Eastern trade, but some amount of trade—is carried on by drawing on consignees for the creation of bills, which bills are discounted in this country; and that trade, which is not of a very healthy description, will always go on, whatever the prices may be.

1401. Do I understand you to mean, in very general terms, that it is difficult to arrest any particular branch of manufacture and export the moment it becomes unprofitable?—Very difficult indeed. In the first place, an amount of fixed capital is sunk in it which has to be moved, and people have formed habits and connections; and such a general cause as I have been speaking of will not operate perhaps for a considerable period of time.

1402. The export trade from this country to another great consuming country might be prolonged sometimes without its being exactly evidence that that export was the result of sound trade and permanent causes?—Quite so; without its being at all a conclusive indication that it was such a trade as ought to be carried on, or such a trade as anybody would begin.

1403. Would the depreciation of silver have this effect,—that it would prevent the extension of business or the initiation of new business while alarm was felt as to the uncertainty of returns through the fluctuations in silver, but it would not cause an immediate cessation and diminution of the trade?—Yes, it would have that effect; it would have a gradual tendency in that direction,—a tendency to make the export trade to India cease.

1404. Turning to another subject,—the evidence before the Committee, I think, has been generally to the effect that the depreciation of silver has been caused by the increased production or the impression produced by the increased production in America, by the demonetization in Germany, and by the increase of the drafts of the Indian Council: do you agree in the existence of these causes?—I think that those causes are real, but I think a fourth ought to be added to them.

1405. What is that fourth cause?—A number of states which are grouped together in what is called the "Latin Union" have ceased to coin silver ever since the year 1874 in the same manner which they did before. As the Committee are aware, the Latin

Union is a name for five states, — France, Belgium, Italy, Switzerland, and Greece, — which up to the year 1874 had what they called a "double standard"; that is to say, silver and gold were tenders for any amount for debts, and the coinage was framed on the relation of 15½ to 1. Up to that time it was open to anybody to go to the French or any other mints, with silver or gold as the case might be, and get it coined. The consequence of course was, that the moment [either] metal became depreciated, the holders took it to those mints and had it coined; but in the year 1874 that process was arrested, because those governments limited the amount of silver which they would coin: and if it had not been for that change of policy, all the silver which is now flooding the London market and lowering the price would have been long since in the mints of those countries; it would have released gold from them, and the combined effect of the two operations would have been, that the comparative value of gold and silver would have been very little altered, — probably not at all.

1406. Without giving an opinion as to whether they did right or wrong in the steps they have taken, do I understand you to mean that their abstention from purchasing, whereas formerly they were buyers, must be added to the effect of the demonetization in Germany? — The operation of the double standard caused a supply on speculation. The moment any one of the two metals becomes depreciated, there is a motive to any bullion dealer to take the depreciated metal to the mint, leave it there, have it coined, and with that he can buy the appreciated metal and have a profit: in that way, in former times, the old silver currency of France was entirely taken away and gold substituted for it, merely because gold was cheaper; in the same way now, if the Latin Union continued to coin as before, gold would have been taken away and silver taken back.

1407. Are you aware that the stock of silver in the Bank of France has increased of late years? — Yes, I am aware that it is now twenty millions or more.

1408. You contend that but for their cessation of coinage, a larger figure than that would have accumulated? — Yes, and gold would have been taken away from them.

1409. To the same amount? — To an equivalent amount, not only of France, but the Latin Union generally.

1410. There has been once or twice before, has there not, in France, a change from silver to gold and from gold to silver? — Yes: we were enabled to pay India in silver for the cotton we wanted during the famine, by getting it from the French currency in this way.

1411. Was France at that time drained of a large portion of its silver currency? — A very large portion. It was the saying in France at that time, "The English have taken away the silver," meaning that we had sent it to India. It was quite true that it was bought up with gold.

1412. Did we pay a premium on silver at the time? — Gold was much depreciated as against the legal equation, just as silver is now against the legal equation, and therefore it was profitable to send gold to the mint.

1413. Had the governments in the Latin Union not curtailed their coinage even before the year 1874? — 1874 is the first year in which they made a treaty on this subject, I think.

1414. Can you state to the Committee any facts with regard to the legislation as to Holland? — It appears to me that the difficulty of Holland in this question is far greater than that of any other country; because they have, as England has, an Indian Empire, and they have the same currency in the Indian Empire as they have at home. They are much in the same position that we should be in if we had a rupee currency here, and we thought of demonetizing rupees. It has been proposed to demonetize the Dutch dollar, which is the coinage both of Holland and of Java, and of other Dutch possessions, which circulates in the East to an enormous extent.

1415. The Dutch dollar has not yet been demonetized? — It has not; but proposals are constantly being made, and an experimental step was made last year towards its demonetization.

1416. Was a bill passed with regard to it? — Yes; but like many experimental measures, it was very complex. I should not like to explain its exact effect; I have had it explained to me in various ways. It was a small act in itself, and only of importance as an indication of a policy which was to follow.

1417. Was it a temporary act or a permanent act? — Temporary.

1418. To cease when? — To cease very soon, I think; but I am not perfectly certain.

1419. As a matter of fact, when that act ceases, will the government of Holland have to make up its mind one way or the other again, and to take some measures? — Either to make a change, or leave things as they are; Holland demonetized gold years ago, and has only a silver currency.

1420. As a matter of fact, without expressing any speculative opinion, they have not yet established a gold valuation? — No; they have greater difficulties in going in that direction than any other country.

1421. I have seen it stated in some publications that Holland was one of those countries that adopted the gold valuation?—That is a complete error; many circumstances much impede them in so doing.

1422. Have they been buying silver or gold latterly, to your knowledge?—I could not lay the details before the Committee.

MR. FAWCETT.

1423. The Latin Union, or the Latin Convention, continues in operation till 1880, does it not?—Till some date of that kind.

1424. Therefore its policy, which you think has been influential in assisting the depreciation of silver, will continue till the time when it ceases, when the confederation breaks up?—Not necessarily: it has an annual meeting, by which it determines the amount of silver which it will coin. I should say that in 1874 they had made a cardinal alteration in their policy; the theory of the double standard is, that any one should be able to bring his money to the mint and get it coined in any amount, but that was altered.

CHAIRMAN.

1425. What was the original policy of the Latin Union?—It was the policy of the double standard, as it is called, in which both gold and silver circulate and are legal tenders for any amount, and in which the relation between them was that of $15\frac{1}{2}$ to 1.

1426. What was the object of their combining?—It was, I suppose, partly a political movement on the part of the French Empire to gain an influence in those countries, and partly the natural wish of countries so intimately connected to have the same coinage; and they adopted the French coinage of that time, as being that of the predominant power.

1427. The Latin Union was not formed with reference at all to the question as between silver and gold?—They simply adopted the French currency of that time.

1428. The policy to suspend the coinage is the common policy that has been adopted by them in the course of their union, but is not one of the principles of their union?—It is contrary to the fundamental principles of their union. They gave up the double standard the moment they allowed their metal to be limited; the cardinal principle was abandoned.

MR. FAWCETT.

1429. Did not they come to some agreement with reference to the coinage of silver, which agreement was to continue in operation

till 1880? I think we have had evidence to that effect.—They met annually, and determined the amount of silver which they should coin.

1430. I think Mr. Giffen gave the evidence, but I fancy we have had evidence to this effect: that when they met in 1874, one of their agreements was, that they should continue a certain policy with regard to the coinage until 1880, and that they should be bound by that agreement until that year?—They re-vote annually what the amount shall be; and it is open now to the annual meeting to change, and to go back to the double standard pure and simple. In 1874 the amount which they agreed to coin was £4,800,000; in 1875 it was raised to £6,000,000, and now it has gone back to £4,800,000 in 1876. It is divided between the countries.

1431. You say they cardinally changed their policy in 1874 with regard to the coinage of silver, and their policy with regard to the future of course is uncertain?—Very uncertain. It is a possibility—I do not say that it is a probability—that they might begin to coin silver in unlimited amounts, and that would take the silver off the market.

1432. On the other hand, it is possible that they may continue this policy, which you think has been influential in assisting the depreciation?—Yes; or they may go further, and demonetize the silver in France. That has been proposed, and that would throw an additional amount of silver on the market.

1433. Their policy one way or the other will have a considerable effect either in promoting the depreciation of silver or in retarding its depreciation; and that policy with regard to the future is, in your opinion, obscure and uncertain?—Yes; it will be a force of the first magnitude.

1434. You would not like, at any rate, positively to predict in what direction that force, which you have described as one of the first magnitude, will operate?—I think there are very great difficulties in the way of demonetizing silver in France: and it is certain, I believe, that the present rulers of France wish to preserve what they call an "expectant attitude," and to continue the present state of things, only coining limited amounts; but whether they will be able so to continue I do not know.

1435. Do you think that one element in considering what the value of silver is, is this,—that the value of the precious metal, after all, is determined by the same considerations as the value of any other mineral or any other commodity, and that consequently the cost of producing those metals, or the cost of raising them, must have an important bearing on their future value?—Undoubtedly.

1436. Therefore, if the cost of producing silver should greatly diminish, that must sooner or later, just in the same way as if the cost of producing any other article greatly diminished, have its effect upon its value? — That will of course have an effect upon the value, but it will be limited by several considerations. One is, that it is the cost of production under the most difficult circumstances which regulates the price; not the cost of production in those mines of splendid fertility which we hear of, but the cost of production in the least of the old mines which keeps itself at work.

1437. To draw an analogy, if you suddenly discovered in a country a great tract of fertile land, the immediate effect of that land being discovered, which would enable agricultural produce to be produced cheaper, would not necessarily be, to lower the value of agricultural produce if the demand for it keep* on increasing, so that it was necessary to keep the (comparatively speaking) unfertile land in cultivation, which before had been cultivated? — Quite so.

1438. But if, on the other hand, this fertile land should so add to agricultural produce that the more unproductive sources of supply which had been before worked, should be given up, then the cost of producing that produce would diminish? —Yes.

1439. You think that would apply as an analogy to the value of the precious metals? —Yes; I think it would be the mine of the least fertility that should keep itself at work, that would regulate the price.

1440. You have described to us very clearly what you think will be the effect on the trade of India, if the depreciation of silver continues; but have you considered what its effect on the revenue of India is? — I suppose that it will be unfavorable to the revenue of India, because the Indian government are so unfortunate as not to be able to increase their taxation.

1441. And the peculiarly unfavorable effect it will produce is [due to] this, — that one considerable portion of the land revenue of India is either permanently or for a considerable period fixed in pecuniary amount, which amount is estimated in silver?† —Yes.

1442. Therefore, although from that circumstance inferences‡ may come into operation to correct any bad effect which it may have on the trade of India, the loss which would arise to the revenue of India from that circumstance cannot be got over by any of

*‡ Evident misprints for "kept" and "influences."— Ed.

† This curious blunder is exactly repeated by Bagehot himself in one of his articles (see *ante*, page 550, last line but one). In both cases I have added the words in brackets to make sense. Of course the fixing of the Indian revenue was not due to the depreciation of silver, as the clumsy wording of Mr. Fawcett's question and Bagehot's editorial imply. — Ed.

the circumstances to which you have referred? — I do not think there is any connection between the trade of India and the revenue of India for this purpose in the peculiar circumstances of the Indian government, because they do not seem to be able to apply additional taxation.

1443. But as to the loss on the revenue, even if they could apply additional taxation :* which is a fixed pecuniary amount, either fixed permanently or for a considerable number of years, — there is no way of meeting that? — No ; that is a matter of agreement which cannot be altered.

SIR CHARLES MILLS.

1444. You mentioned the demonetization of silver by Germany as being one of the causes : I suppose you will supplement that by the cessation of the demand for fresh coinage? — Quite so.

1445. It includes not only the selling of the silver, but also the cessation of the demand for fresh silver? — Yes.

1446. You stated that you thought it was very difficult to form any opinion as to the amount of silver and gold there was in circulation in the world : I think you go further, do you not, and say it is very difficult to form even an opinion as to the amount of gold in circulation in England? — There are very various estimates by very competent persons. Of course it is much more possible to get near that than the circulation of the world, but such estimates are more matters of scientific conjecture than anything else.

1447. We had some figures given us as to the amount of thalers in Germany : do you think that those are also very doubtful? — Very dubious indeed. I have a strong belief that the government do not themselves know ; their whole policy is perplexed by uncertainty as to that, as far as an external observer can judge.

CHAIRMAN.

1448. When you speak of the drafts of the government of India, you consider that those drafts, I presume, are determined by the amount that they require : it is not an open question how much money they can raise, or how much they need not raise? — I suppose that the drafts are regulated by the necessities of the Indian government at home : they have a certain interest to pay, certain salaries to discharge, and certain things to buy, which are absolute necessities, I suppose.

1449. You do not wish to convey the idea, when you stated, as other witnesses have stated, that the increase in the drafts of the

*Some words like "the land tax," are evidently omitted here. — ED.

Indian Council is one of the causes which have led to the depreciation of silver, that it was at all a cause which the Indian government could have avoided?—I apprehend it is not optional at all.

MR. FAWCETT.

1450. The great part of the expenditure of India is quite within the control of the Home government here. I will give one illustration. For instance, so much had to be remitted from India to England for the payment for the buildings at the India Office: it was perfectly optional with the Government here whether they erected buildings. I do not mean to say whether they were wise in erecting the buildings they have, but it was optional for them to spend more or less or the exact amount which they did spend on those buildings. Therefore the expenditure is within their control; but having sanctioned a certain expenditure, of course the amount they have to withdraw is not within their control?—Yes, it is only in that sense optional. Having determined their expenditure by political considerations, the money must come.

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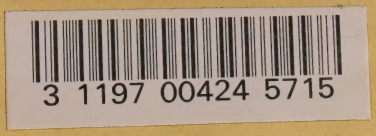
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